

CITIZENS INC
Form 10-Q
May 06, 2011

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

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2011

or

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

Commission File Number: 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. Yes No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting
company

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

As of May 4, 2011, the Registrant had 48,689,341 shares of Class A common stock, no par value, outstanding and 1,001,714 shares of Class B common stock outstanding.

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. FINANCIAL STATEMENTS****CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES****Consolidated Statements of Financial Position****(In thousands)**

| | March 31, 2011 (Unaudited) | December 31, 2010 |
|--|---|------------------------------|
| Assets | | |
| Investments: | | |
| Fixed maturities available-for-sale, at fair value (cost: \$622,282 and \$578,412 in 2011 and 2010, respectively) | \$ 620,614 | 575,737 |
| Fixed maturities held-to-maturity, at amortized cost (fair value: \$65,611 and \$79,103 in 2011 and 2010, respectively) | 67,078 | 80,232 |
| Equity securities available-for-sale, at fair value (cost: \$19,729 and \$19,844 in 2011 and 2010, respectively) | 23,815 | 23,304 |
| Mortgage loans on real estate | 1,478 | 1,489 |
| Policy loans | 36,306 | 35,585 |
| Real estate held for investment (less \$1,049 and \$1,017 accumulated depreciation in 2011 and 2010, respectively) | 9,168 | 9,200 |
| Other long-term investments | 146 | 148 |
| Total investments | 758,605 | 725,695 |
| Cash and cash equivalents | 37,450 | 49,723 |
| Accrued investment income | 8,432 | 7,433 |
| Reinsurance recoverable | 9,397 | 9,729 |
| Deferred policy acquisition costs | 128,325 | 125,684 |
| Cost of customer relationships acquired | 30,962 | 31,631 |
| Goodwill | 17,160 | 17,160 |
| Other intangible assets | 1,012 | 1,019 |
| Federal income tax receivable | | 1,914 |
| Property and equipment, net | 7,389 | 7,101 |
| Due premiums, net (less \$1,498 and \$1,568 allowance for doubtful accounts in 2011 and 2010, respectively) | 8,184 | 8,537 |
| Prepaid expenses | 1,850 | 474 |
| Other assets | 728 | 406 |
| Total assets | \$ 1,009,494 | 986,506 |

See accompanying notes to consolidated financial statements.

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

| | March 31, 2011 (Unaudited) | December 31, 2010 |
|---|---|------------------------------|
| Liabilities and Stockholders' Equity | | |
| Liabilities: | | |
| Policy liabilities: | | |
| Future policy benefit reserves: | | |
| Life insurance | \$ 649,030 | 637,140 |
| Annuities | 43,071 | 42,096 |
| Accident and health | 5,705 | 5,910 |
| Dividend accumulations | 9,817 | 9,498 |
| Premiums paid in advance | 24,399 | 23,675 |
| Policy claims payable | 10,815 | 10,540 |
| Other policyholders' funds | 8,085 | 8,191 |
| | | |
| Total policy liabilities | 750,922 | 737,050 |
| Commissions payable | 2,363 | 2,538 |
| Federal income tax payable | 128 | |
| Deferred federal income tax | 9,806 | 9,410 |
| Payable for securities in process of settlement | 5,973 | |
| Warrants outstanding | 1,188 | 1,587 |
| Other liabilities | 8,655 | 8,287 |
| | | |
| Total liabilities | 779,035 | 758,872 |
| | | |
| 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 2011 and 2010, including shares in treasury of 3,135,738 in 2011 and 2010 | 256,703 | 256,703 |
| Class B, no par value, 2,000,000 shares authorized, 1,001,714 shares issued and outstanding in 2011 and 2010 | 3,184 | 3,184 |
| Accumulated deficit | (20,801) | (22,581) |
| Accumulated other comprehensive income: | | |
| Unrealized gains on securities, net of tax | 2,384 | 1,339 |
| | | |
| Treasury stock, at cost | 241,470 (11,011) | 238,645 (11,011) |
| | | |
| Total stockholders' equity | 230,459 | 227,634 |
| | | |
| Total liabilities and stockholders' equity | \$ 1,009,494 | 986,506 |

See accompanying notes to consolidated financial statements.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Operations
Three Months Ended March 31,
(In thousands, except per share amounts)
(Unaudited)

| | 2011 | 2010 |
|---|-----------------|---------------|
| Revenues: | | |
| Premiums: | | |
| Life insurance | \$ 35,611 | 33,596 |
| Accident and health insurance | 372 | 414 |
| Property insurance | 1,245 | 1,180 |
| Net investment income | 7,514 | 8,349 |
| Realized gains (losses), net | 19 | 59 |
| Decrease (increase) in fair value of warrants | 399 | (114) |
| Other income | 123 | 348 |
| Total revenues | 45,283 | 43,832 |
| Benefits and expenses: | | |
| Insurance benefits paid or provided: | | |
| Claims and surrenders | 14,879 | 15,577 |
| Increase in future policy benefit reserves | 12,318 | 9,545 |
| Policyholders dividends | 1,662 | 1,570 |
| Total insurance benefits paid or provided | 28,859 | 26,692 |
| Commissions | 9,072 | 8,128 |
| Other underwriting, acquisition and insurance expenses | 6,610 | 6,853 |
| Capitalization of deferred policy acquisition costs | (7,165) | (5,995) |
| Amortization of deferred policy acquisition costs | 4,520 | 4,944 |
| Amortization of cost of customer relationships acquired and other intangibles | 654 | 838 |
| Total benefits and expenses | 42,550 | 41,460 |
| Income before federal income tax | 2,733 | 2,372 |
| Federal income tax expense (benefit) | 953 | 767 |
| Net income (loss) | \$ 1,780 | 1,605 |
| Net income (loss) applicable to common stockholders | \$ 1,780 | 1,605 |
| Per Share Amounts: | | |
| Basic earnings per share of Class A common stock | \$ 0.04 | 0.03 |
| Basic earnings per share of Class B common stock | \$ 0.02 | 0.02 |

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| | | | |
|--|----|------|------|
| Diluted earnings per share of Class A common stock | \$ | 0.03 | 0.03 |
| Diluted earnings per share of Class B common stock | \$ | 0.01 | 0.02 |

See accompanying notes to consolidated financial statements.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Cash Flows
Three Months Ended March 31,
(In thousands)
(Unaudited)

| | 2011 | 2010 |
|---|-------------|-------------|
| Cash flows from operating activities: | | |
| Net income | \$ 1,780 | 1,605 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Net realized losses (gains) on sale of investments and other assets | (19) | (59) |
| Net deferred policy acquisition costs | (2,645) | (1,051) |
| Amortization of cost of customer relationships acquired and other intangibles | 654 | 838 |
| Increase (decrease) in fair value of warrants | (399) | 114 |
| Depreciation | 205 | 274 |
| Amortization of premiums and discounts on fixed maturities and short-term investments | 1,240 | 585 |
| Deferred federal income tax benefit | (166) | (995) |
| Change in: | | |
| Accrued investment income | (999) | (1,227) |
| Reinsurance recoverable | 332 | 241 |
| Due premiums | 353 | 560 |
| Future policy benefit reserves | 12,100 | 9,339 |
| Other policyholders' liabilities | 1,212 | 1,401 |
| Federal income tax receivable | 2,042 | 2,633 |
| Commissions payable and other liabilities | 193 | (1,054) |
| Other, net | (1,554) | (590) |
| Net cash provided by (used in) operating activities | 14,329 | 12,614 |
| Cash flows from investing activities: | | |
| Purchase of fixed maturities, held-to-maturity | (5,973) | (4,095) |
| Calls of fixed maturities, held-to-maturity | 19,000 | 8,000 |
| Sale of fixed maturities, available-for-sale | | 2,126 |
| Maturity and calls of fixed maturities, available-for-sale | 8,871 | 29,216 |
| Purchase of fixed maturities, available-for-sale | (47,922) | (49,643) |
| Sale of equity securities, available-for-sale | | 104 |
| Calls of equity securities, available-for-sale | 150 | |
| Purchase of equity securities, available-for-sale | | (49) |
| Principal payments on mortgage loans | 11 | 13 |
| Increase in policy loans | (721) | (986) |
| Sale of other long-term investments and property and equipment | 1 | |
| Purchase of other long-term investments and property and equipment | (579) | (834) |
| Maturity of short-term investments | | 2,500 |
| Net cash provided by (used in) investing activities | (27,162) | (13,648) |

See accompanying notes to consolidated financial statements.

(Continued)

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Consolidated Statements of Cash Flows, Continued
Three Months Ended March 31,
(In thousands)
(Unaudited)

| | 2011 | 2010 |
|--|-------------|-------------|
| Cash flows from financing activities: | | |
| Annuity deposits | \$ 1,560 | 1,197 |
| Annuity withdrawals | (1,000) | (765) |
| Net cash provided by (used in) financing activities | 560 | 432 |
| Net increase (decrease) in cash and cash equivalents | (12,273) | (602) |
| Cash and cash equivalents at beginning of year | 49,723 | 48,625 |
| Cash and cash equivalents at end of period | \$ 37,450 | 48,023 |
| Supplemental disclosures of operating activities: | | |
| Cash paid (recovered) during the period for income taxes | \$ (923) | (871) |

Supplemental Disclosures of Non-Cash Investing Activities:

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

See accompanying notes to consolidated financial statements.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements
March 31, 2011
(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), 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 March 31, 2011, the consolidated statements of operations for the three-month periods ended March 31, 2011 and 2010, and the consolidated statements of cash flows for the three-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 March 31, 2011 and for comparative periods have been made.

We provide primarily, life insurance policies through four of our subsidiaries CICA, SPLIC, CNLIC and ICIC as well as a small amount of health insurance policies through CICA and CNLIC. 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.

The Company recorded adjustments in the current quarter of 2011 related to the reserve calculation of certain SPLIC policies as of December 31, 2010 that resulted in a pre-tax decrease in reserves of \$0.2 million. In addition, the Company utilized system generated information to refine estimates from December 31, 2010, which resulted in a decrease of deferred acquisition costs of \$0.3 million and a reserve decrease of \$0.1 million reflected in the current reporting period. The resulting net income impact totaled \$50,237 in the current period.

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 and equity 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.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements
March 31, 2011
(Unaudited)

Reclassification

The Company recorded reclassifications related to DAC amounts capitalized and amortized to properly reflect the amount used to develop the DAC asset balance and to provide consistent presentation with the current year. We recorded an increase to DAC capitalized of \$0.6 million and an increase in amortization for the same amount for the first quarter of 2010. The Company also recorded a reclassification of \$0.1 million from other underwriting, acquisitions and insurance expenses to claims and surrenders relating to a legal settlement on a reinsured accident and health policy for the first quarter of 2010.

Significant Accounting Policies

For a description of significant accounting policies, see Note 1 of the Notes to Consolidated Financial Statements included in our 2010 Form 10-K Annual Report, which should be read in conjunction with these accompanying Consolidated Financial Statements.

(2) Accounting Pronouncements

Accounting Standards Not Yet Adopted

In October 2010, the FASB issued guidance modifying the definition of the types of costs incurred by insurance entities that can be capitalized in the acquisition of new and renewal contracts. The guidance specifies that the costs must be based on successful efforts. The guidance also specifies that advertising costs should be included as deferred acquisition costs only when the direct-response advertising accounting criteria are met. If application of the guidance would result in the capitalization of acquisition costs that had not been capitalized prior to adoption, the entity may elect not to capitalize those additional costs. The new guidance is effective for reporting periods beginning after December 15, 2011 and should be applied prospectively, with retrospective application permitted. The Company is in the process of evaluating the impact of adoption of the guidance on the results of operations and financial position.

Accounting Standards Recently Adopted

In December 2010, the FASB issued disclosure guidance for entities that enter into business combinations that are material. The guidance specifies that if an entity presents comparative financial statements, the entity should disclose pro forma revenue and earnings of the combined entity as though the business combination that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The guidance expands the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination. The Company will apply the guidance to any business combinations entered into on or after January 1, 2011.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements (Continued)
March 31, 2011
(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 March 31, 2011 | | | |
|---|--|-----------------------|----------------------|---------------------|
| | Life | Home | Other | |
| | Insurance | Service | Non-Insurance | Consolidated |
| | | Insurance | Enterprises | |
| | | (In thousands) | | |
| Revenues: | | | | |
| Premiums | \$ 26,520 | 10,708 | | 37,228 |
| Net investment income | 4,081 | 3,237 | 196 | 7,514 |
| Realized gains (losses), net | | 19 | | 19 |
| Decrease (increase) in fair value of warrants | | | 399 | 399 |
| Other income | 87 | 8 | 28 | 123 |
| Total revenue | 30,688 | 13,972 | 623 | 45,283 |
| Benefits and expenses: | | | | |
| Insurance benefits paid or provided: | | | | |
| Claims and surrenders | 9,401 | 5,478 | | 14,879 |
| Increase in future policy benefit reserves | 11,809 | 509 | | 12,318 |
| Policyholders dividends | 1,643 | 19 | | 1,662 |
| Total insurance benefits paid or provided | 22,853 | 6,006 | | 28,859 |
| Commissions | 5,342 | 3,730 | | 9,072 |
| Other underwriting, acquisition and insurance expenses | 2,954 | 3,082 | 574 | 6,610 |
| Capitalization of deferred policy acquisition costs | (5,427) | (1,738) | | (7,165) |
| Amortization of deferred policy acquisition costs | 3,838 | 682 | | 4,520 |
| Amortization of cost of customer relationships acquired and other intangibles | 223 | 431 | | 654 |
| Total benefits and expenses | 29,783 | 12,193 | 574 | 42,550 |
| Income (loss) before income tax expense | \$ 905 | 1,779 | 49 | 2,733 |

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements (Continued)
March 31, 2011
(Unaudited)

| | Three Months Ended March 31, 2010 | | | Consolidated |
|---|--|---------------------------------------|--|-----------------------|
| | Life Insurance | Home Service Insurance | Other Non-Insurance Enterprises | |
| | | | | |
| | | | | (In thousands) |
| Revenues: | | | | |
| Premiums | \$ 24,769 | 10,421 | | 35,190 |
| Net investment income | 4,711 | 3,532 | 106 | 8,349 |
| Realized gains (losses), net | (29) | 133 | (45) | 59 |
| Decrease (increase) in fair value of warrants | | | (114) | (114) |
| Other income | 277 | 49 | 22 | 348 |
| Total revenue | 29,728 | 14,135 | (31) | 43,832 |
| | | | | |
| Benefits and expenses: | | | | |
| Insurance benefits paid or provided: | | | | |
| Claims and surrenders | 9,899 | 5,678 | | 15,577 |
| Increase in future policy benefit reserves | 8,662 | 883 | | 9,545 |
| Policyholders dividends | 1,542 | 28 | | 1,570 |
| Total insurance benefits paid or provided | 20,103 | 6,589 | | 26,692 |
| | | | | |
| Commissions | 4,505 | 3,623 | | 8,128 |
| Other underwriting, acquisition and insurance expenses | 2,977 | 3,641 | 235 | 6,853 |
| Capitalization of deferred policy acquisition costs | (4,464) | (1,531) | | (5,995) |
| Amortization of deferred policy acquisition costs | 4,659 | 285 | | 4,944 |
| Amortization of cost of customer relationships acquired and other intangibles | 330 | 508 | | 838 |
| Total benefits and expenses | 28,110 | 13,115 | 235 | 41,460 |
| | | | | |
| Income (loss) before income tax expense | \$ 1,618 | 1,020 | (266) | 2,372 |

(4) Total Comprehensive Income

**Three Months Ended March
31,
2011 2010**
(In thousands)

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| | | | |
|--|----|-------|---------|
| Net income (loss) | \$ | 1,780 | 1,605 |
| Other comprehensive income net of effects of deferred acquisition costs and taxes: | | | |
| Unrealized gains (losses) on available-for-sale securities | | 1,607 | 6,451 |
| Tax (expense) benefit | | (562) | (1,789) |
| Other comprehensive income (loss) | | 1,045 | 4,662 |
| Total comprehensive income (loss) | \$ | 2,825 | 6,267 |

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements (Continued)
March 31, 2011
(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 March 31, | |
|--|---|-------------|
| | 2011 | 2010 |
| | (In thousands, except per share amounts) | |
| Basic and diluted earnings per share: | | |
| Numerator: | | |
| Net income allocated to Class A common stock | \$ 1,762 | 1,589 |
| Net income allocated to Class B common stock | 18 | 16 |
| Net income available to common stockholders | \$ 1,780 | 1,605 |
| Denominator: | | |
| Weighted average shares of Class A outstanding - basic | 48,687 | 48,686 |
| Weighted average shares of Class B outstanding - basic and diluted | 1,002 | 1,002 |
| Total weighted average shares outstanding - basic | 49,689 | 49,688 |
| Basic earnings per share of Class A common stock | \$ 0.04 | 0.03 |
| Basic earnings per share of Class B common stock | \$ 0.02 | 0.02 |
| Diluted earnings per share of Class A common stock | \$ 0.03 | 0.03 |
| Diluted earnings per share of Class B common stock | \$ 0.01 | 0.02 |

For the three months ended March 31, 2011, certain warrants associated with the Convertible Preferred Stock portfolio became dilutive. As such, the diluted weighted average shares of Class A common stock outstanding for the period was 48,731,000.

For the three months ended March 31, 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 for the period was 48,686,000.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements (Continued)
March 31, 2011
(Unaudited)

(6) Investments

The Company invests primarily in fixed maturity securities, which totaled 86.3% of total investments and cash and cash equivalents at March 31, 2011.

| | March 31, 2011 | | December 31, 2010 | |
|---|-----------------------|-------------------|--------------------------|-------------------|
| | Carrying | % of Total | Carrying | % of Total |
| | Value | Carrying | Value | Carrying |
| | (In | Value | (In | Value |
| | thousands) | | thousands) | |
| Fixed maturity securities | \$ 687,692 | 86.3% | \$ 655,969 | 84.6% |
| Equity securities | 23,815 | 3.0 | 23,304 | 3.0 |
| Mortgage loans | 1,478 | 0.2 | 1,489 | 0.2 |
| Policy loans | 36,306 | 4.6 | 35,585 | 4.6 |
| Real estate and other long-term investments | 9,314 | 1.2 | 9,348 | 1.2 |
| Cash and cash equivalents | 37,450 | 4.7 | 49,723 | 6.4 |
| Total cash, cash equivalents and investments | \$ 796,055 | 100.0% | \$ 775,418 | 100.0% |

Cash balances decreased in 2011 compared to December 31, 2010 as available funds were invested into fixed maturity securities.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
Notes to Consolidated Financial Statements (Continued)
March 31, 2011
(Unaudited)

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

| | Cost or Amortized Cost | March 31, 2011 | | Fair Value |
|--|------------------------------|------------------------------|-------------------------------|---------------|
| | | Gross Unrealized Gains | Gross Unrealized Losses | |
| (In thousands) | | | | |
| Fixed maturities available-for-sale: | | | | |
| U.S. Treasury securities | \$ 10,469 | 1,759 | 1 | 12,227 |
| U.S. Government-sponsored enterprises States of the United States and political subdivisions of the states | 312,801 | 372 | 6,911 | 306,262 |
| Foreign governments | 127,659 | 817 | 4,748 | 123,728 |
| Corporate | 105 | 25 | | 130 |
| Securities not due at a single maturity date | 158,591 | 7,187 | 926 | 164,852 |
| | 12,657 | 776 | 18 | 13,415 |
| Total fixed maturities available-for-sale | 622,282 | 10,936 | 12,604 | 620,614 |
| Fixed maturities held-to-maturity: | | | | |
| U.S. Government-sponsored enterprises | 67,078 | 118 | 1,585 | 65,611 |
| Total fixed maturities | \$ 689,360 | 11,054 | 14,189 | 686,225 |
| Total equity securities | \$ 19,729 | 4,086 | | 23,815 |

| | Cost or Amortized Cost | December 31, 2010 | | Fair Value |
|--|------------------------------|------------------------------|-------------------------------|---------------|
| | | Gross Unrealized Gains | Gross Unrealized Losses | |
| (In thousands) | | | | |
| Fixed maturities available-for-sale: | | | | |
| U.S. Treasury securities | \$ 10,908 | 1,917 | | 12,825 |
| U.S. Government-sponsored enterprises States of the United States and political subdivisions of the states | 290,904 | 441 | 6,390 | 284,955 |
| Foreign governments | 107,214 | 539 | 6,034 | 101,719 |
| Corporate | 106 | 26 | | 132 |
| Securities not due at a single maturity date | 155,277 | 7,237 | 1,216 | 161,298 |
| | 14,003 | 833 | 28 | 14,808 |
| Total fixed maturities available-for-sale | 578,412 | 10,993 | 13,668 | 575,737 |
| Fixed maturities held-to-maturity: | | | | |
| U.S. Government-sponsored enterprises | 80,232 | 272 | 1,401 | 79,103 |
| Total fixed maturities | \$ 658,644 | 11,265 | 15,069 | 654,840 |

| | | | | |
|-------------------------|----|--------|-------|--------|
| Total equity securities | \$ | 19,844 | 3,460 | 23,304 |
|-------------------------|----|--------|-------|--------|

Almost 93% or \$11.7 million of the Company's mortgage-backed security holdings totaling \$12.7 million are residential U.S. Government-sponsored issues. 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 diversified mutual funds.

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 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.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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(Unaudited)

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 did not recognize any other-than-temporary impairments (OTTI) items during the quarters ended March 31, 2011 and March 31, 2010.

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(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.

| | March 31, 2011 | | | | | | | | |
|--|---------------------|-------------------|-----------------|------------------------|-------------------|-----------------|------------|-------------------|-----------------|
| | 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. Treasury securities | \$ 101 | 1 | 1 | | | | 101 | 1 | 1 |
| U.S. Government-sponsored enterprises | 258,396 | 6,911 | 185 | | | | 258,396 | 6,911 | 185 |
| Securities issued by states and political subdivisions | 66,177 | 2,113 | 56 | 9,753 | 2,635 | 8 | 75,930 | 4,748 | 64 |
| Corporate | 21,417 | 743 | 17 | 3,070 | 183 | 3 | 24,487 | 926 | 20 |
| Securities not due at a single maturity date | 86 | | 1 | 186 | 18 | 4 | 272 | 18 | 5 |
| Total available-for-sale | 346,177 | 9,768 | 260 | 13,009 | 2,836 | 15 | 359,186 | 12,604 | 275 |
| Held-to-maturity securities: | | | | | | | | | |
| U.S. Government-sponsored enterprises | 49,462 | 1,585 | 24 | | | | 49,462 | 1,585 | 24 |
| Total fixed maturities | \$ 395,639 | 11,353 | 284 | 13,009 | 2,836 | 15 | 408,648 | 14,189 | 299 |

| | December 31, 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 | \$ 234,994 | 6,390 | 170 | | | | 234,994 | 6,390 | 170 |
| Securities issued by states and political subdivisions | 66,836 | 3,270 | 60 | 9,626 | 2,764 | 8 | 76,462 | 6,034 | 68 |
| Corporate | 28,072 | 1,040 | 21 | 2,443 | 176 | 7 | 30,515 | 1,216 | 28 |
| Securities not due at a single maturity date | 569 | 8 | 2 | 201 | 20 | 5 | 770 | 28 | 7 |
| Total available-for-sale | 330,471 | 10,708 | 253 | 12,270 | 2,960 | 20 | 342,741 | 13,668 | 273 |
| Held-to-maturity securities: | | | | | | | | | |
| | 45,699 | 1,401 | 18 | | | | 45,699 | 1,401 | 18 |

U.S. Government-sponsored
enterprises

| | | | | | | | | | |
|------------------------|------------|--------|-----|--------|-------|----|---------|--------|-----|
| Total fixed maturities | \$ 376,170 | 12,109 | 271 | 12,270 | 2,960 | 20 | 388,440 | 15,069 | 291 |
|------------------------|------------|--------|-----|--------|-------|----|---------|--------|-----|

As of March 31, 2011 and December 31, 2010, there are no unrealized losses on the Company's equity securities.

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As of March 31, 2011, the Company had 15 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.

The amortized cost and fair value of fixed maturity securities at March 31, 2011 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.

| | March 31, 2011 | |
|--|---------------------------|-----------------------|
| | Amortized Cost | Fair Value |
| | (In thousands) | |
| Available-for-sale securities: | | |
| Due in one year or less | \$ 61,192 | 60,053 |
| Due after one year through five years | 40,264 | 41,690 |
| Due after five years through ten years | 113,821 | 115,003 |
| Due after ten years | 394,348 | 390,453 |
| Total available-for-sale securities | 609,625 | 607,199 |
| Held-to-maturity securities: | | |
| Due after ten years | 67,078 | 65,611 |
| Securities not due at a single maturity date | 12,657 | 13,415 |
| Total fixed maturities | \$ 689,360 | 686,225 |

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 months ended March 31, 2011 and 2010 are summarized as follows:

| | Fixed Maturities Available-for-Sale Three Months Ended March 31, | | Equity Securities Three Months Ended March 31, | |
|----------------------|---|-------------|---|-------------|
| | 2011 | 2010 | 2011 | 2010 |
| | (In thousands) | | (In thousands) | |
| Proceeds | \$ | 2,126 | \$ | 104 |
| Gross realized gains | \$ | 127 | \$ | 25 |

No securities were sold for realized losses or sold from the held-to-maturity portfolio during the three months ended March 31, 2011 or 2010.

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(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.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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March 31, 2011
(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 | | | Total Fair Value |
|---|--------------------------------|----------------|----------------|-----------------------------|
| | Level 1 | Level 2 | Level 3 | |
| | March 31, 2011 | | | |
| | (In thousands) | | | |
| Financial assets: | | | | |
| Fixed maturities available-for-sale: | | | | |
| U.S. Treasury and U.S. Government-sponsored enterprises | \$ 12,227 | 306,262 | | 318,489 |
| Corporate | | 164,852 | | 164,852 |
| Municipal bonds | | 123,728 | | 123,728 |
| Mortgage-backed | | 12,917 | 498 | 13,415 |
| Foreign governments | | 130 | | 130 |
| Total fixed maturities, available-for-sale | 12,227 | 607,889 | 498 | 620,614 |
| Total equity securities, available-for-sale | 23,815 | | | 23,815 |
| Total financial assets | \$ 36,042 | 607,889 | 498 | 644,429 |
| Financial liabilities: | | | | |
| Warrants outstanding | \$ | 1,188 | | 1,188 |

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 | | | Total Fair Value |
|---|--------------------------------|----------------|----------------|-----------------------------|
| | Level 1 | Level 2 | Level 3 | |
| | December 31, 2010 | | | |
| | (In thousands) | | | |
| Financial assets: | | | | |
| Fixed maturities available-for-sale: | | | | |
| U.S. Treasury and U.S. Government-sponsored enterprises | \$ 12,825 | 284,955 | | 297,780 |
| Corporate | | 161,298 | | 161,298 |
| Municipal bonds | | 101,719 | | 101,719 |
| Mortgage-backed | | 14,289 | 519 | 14,808 |
| Foreign governments | | 132 | | 132 |
| Total fixed maturities, available-for-sale | 12,825 | 562,393 | 519 | 575,737 |
| Total equity securities, available-for-sale | 23,304 | | | 23,304 |
| Total financial assets | \$ 36,129 | 562,393 | 519 | 599,041 |

Financial liabilities:

| | | | |
|----------------------|----|-------|-------|
| Warrants outstanding | \$ | 1,587 | 1,587 |
|----------------------|----|-------|-------|

Financial Instruments Valuation

Fixed maturity securities, available-for-sale. At March 31, 2011, the fixed maturities, valued using a third-party pricing source, totaled \$607.9 million for Level 2 assets and comprised 94.3% 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 three months ended March 31, 2011, 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.

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

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

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:

| | Three Months Ended March | |
|--|---------------------------------|-------------|
| | 31, | |
| | 2011 | 2010 |
| | (In thousands) | |
| Balance at beginning of period | \$ 519 | 577 |
| Total realized and unrealized losses: | | |
| Included in net income | | |
| Included in other comprehensive income | (1) | (1) |
| Principal paydowns | (20) | (14) |
| Transfer in and (out) of Level 3 | | |
| Balance at end of period | \$ 498 | 562 |

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:

| | March 31, 2011 | | December 31, 2010 | |
|------------------------------------|-----------------------|--------------|--------------------------|--------------|
| | Carrying | Fair | Carrying | Fair |
| | Value | Value | Value | Value |
| | (In thousands) | | | |
| Financial assets: | | | | |
| Fixed maturities, held-to-maturity | \$ 67,078 | 65,611 | 80,232 | 79,103 |
| Mortgage loans | 1,478 | 1,430 | 1,489 | 1,433 |
| Policy loans | 36,306 | 36,306 | 35,585 | 35,585 |
| Cash and cash equivalents | 37,450 | 37,450 | 49,723 | 49,723 |
| Financial liabilities: | | | | |
| Annuities | 43,071 | 40,893 | 42,096 | 38,619 |

Fair values for fixed income securities are based on quoted market prices. In cases where quoted market prices are not available, fair values are based on estimates using present value or other assumptions, including the

discount rate and estimates of future cash flows.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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Mortgage loans are secured principally by residential and commercial properties. Weighted average interest rates for these loans were approximately 6.7% per year as of March 31, 2011 and December 31, 2010, with maturities ranging from one to thirty years.

Policy loans have a weighted average annual interest rate of 7.7% as of March 31, 2011 and December 31, 2010, 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 at or above the crediting rate applied to the related policy and contract reserves. Policy loans are an integral part of the life insurance policies we have in force and cannot be valued separately and are not marketable; therefore, the fair value of policy loans approximates the carrying value.

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 March 31, 2011 using discounted cash flows. 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 *Delia Bolanos Andrade, et al., Plaintiffs, v. Citizens Insurance Company of America, et al., Defendants* 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.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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(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. The investors were also issued unit warrants to purchase Series A-2 Convertible Preferred Stock. In 2005, three of the four investors exercised their right to purchase the Series A-2 Convertible Preferred Stock. 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.

There are outstanding warrants to purchase the Company's stock at prices ranging from \$6.72 to \$7.93, which were issued to investors of the Class A-1 and A-2 preferred stock. There are 1,022,471 warrants to purchase stock that expire, if not exercised, on July 12, 2011 and 178,969 that expire, if not exercised, at various dates in the third quarter of 2012. The fair value of the warrants is calculated using the Black-Scholes option pricing model and is classified as a liability on the balance sheet in the amount of \$1.2 million and \$1.6 million at March 31, 2011 and December 31, 2010, respectively. The change in fair value of warrants is reported as a component of revenue in the income statement. The change in fair value of warrants for the three months ended March 31 caused an increase in revenues of \$0.4 million and a decrease of \$0.1 million in 2011 and 2010, respectively.

(10) Income Taxes

The effective tax rate was 34.9% and 32.3% for the first quarter of 2011 and 2010, respectively. The 2011 and 2010 rates were lower than the statutory rate of 35%, primarily due to gains and losses from the change in fair value of outstanding warrants for the purchase of Class A common stock. The change in fair value of outstanding warrants, which is not taxable, resulted in an increase to income of \$0.4 million and a decrease of \$0.1 million for the three months ended March 31, 2011 and 2010, respectively.

(11) Related Party Transactions

The Company has filed a plan of merger with the Departments of Insurance of Colorado and Indiana related to the planned dissolution of ICC and the merger of the down-line subsidiary ICIC into CICA. Currently, ICC is owned 87% by Citizens, Inc. and 13% by CICA. This merger will not impact the overall consolidated financials of the Company. The Company does anticipate the elimination of duplicative overhead and annual regulatory reporting expenses once the merger is completed.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES

March 31, 2011

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, 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;

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.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Overview

Citizens, Inc. is an insurance holding company serving the life insurance needs of individuals in the United States since 1969 and internationally since 1975. Through our insurance subsidiaries, we pursue a strategy of offering traditional insurance products in niche markets where we believe we are able to achieve competitive advantages. We had approximately \$1.0 billion of assets under management at March 31, 2011 and December 31, 2010 and approximately \$5.1 billion of insurance in force. Our core insurance 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, principally in Latin America and the Pacific Rim, through independent marketing consultants;

ordinary whole life insurance policies to middle income households concentrated in the midwest and southern United States through independent marketing consultants; and

final expense and limited liability property policies to middle and lower income households in Louisiana, Arkansas, and Mississippi through employee and independent agents in our home service distribution channel.

We were formed in 1969 by our Chairman, Harold E. Riley. Prior to our formation, Mr. Riley had many years of experience in the international and domestic life insurance business. Our Company has experienced significant growth through acquisitions in the domestic market and through market expansion in the international market. We capitalize on the experience of our management team in marketing and operations as we seek to generate bottom line return using knowledge of our niche markets and our well-established distribution channels. We believe our underwriting processes, policy terms, pricing practices and proprietary administrative systems enable us to be competitive in our current markets while protecting our shareholders and servicing our policyholders.

Current Financial Results

Revenues rose from \$43.8 million as of March 31, 2010 to \$45.3 million for the three months ended 2011. Our assets grew from \$986.5 million as of December 31, 2010 to \$1.0 billion as of March 31, 2011. Total stockholders' equity increased from \$227.6 million at December 31, 2010 to \$230.5 million at March 31, 2011.

Our Operating Segments

Our business is comprised of three operating business segments, as detailed below.

Life Insurance

Home Service Insurance

Other Non-insurance Enterprises

Our insurance operations are the primary focus of the Company as those segments generate the majority of our income. See the discussion under Segment Operations for detailed analysis. The amount of insurance, number of policies, and average policy face amounts of policies issued during the periods indicated are shown below.

| | Three Months Ended March 31, | | | | | |
|--------------------|-------------------------------------|---------------|----------------|------------------|-----------------|----------------|
| | 2011 | 2011 | Average | 2010 | 2010 | Average |
| Amount of | Number | of | Policy | Amount of | Number | Average |
| Insurance | Policies | Policy | Face | Insurance | Policies | Policy |
| Issued | Issued | Amount | Amount | Issued | Issued | Amount |
| Issued | Issued | Issued | Issued | Issued | Issued | Issued |
| International Life | 85,479,318 | 1,258 | \$ 67,900 | 66,221,613 | 970 | \$ 69,519 |
| Domestic Life | 2,116,239 | 105 | 20,543 | 2,453,817 | 123 | 20,483 |
| Home Service | 59,463,098 | 8,065 | 7,221 | 55,988,544 | 7,252 | 7,495 |

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Note: All discussion below compares or states 2011 results for the first quarter compared to 2010 results.

Consolidated Results of Operations**Revenues**

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

| | Three Months Ended March | |
|---|---------------------------------|-------------|
| | 31, | |
| | 2011 | 2010 |
| | (In thousands) | |
| Revenues: | | |
| Premiums: | | |
| Life insurance | \$ 35,611 | 33,596 |
| Accident and health insurance | 372 | 414 |
| Property insurance | 1,245 | 1,180 |
| Net investment income | 7,514 | 8,349 |
| Realized gains, net | 19 | 59 |
| Decrease (increase) in fair value of warrants | 399 | (114) |
| Other income | 123 | 348 |
| | | |
| Total revenues | 45,283 | 43,832 |
| Exclude increase (decrease) in fair value of warrants | (399) | 114 |
| | | |
| Total revenues excluding fair value adjustments | \$ 44,884 | 43,946 |

Premium Income. Life insurance premium revenue grew 6.0% from 2010 levels, primarily related to increases in international and home service sales. Marketing efforts in these segments have contributed to an increase in first year sales as well as the fact that renewal premiums increased from improved policy persistency. Similarly, our property insurance premiums in the current period have increased due to a rate increase of 5.7% that became effective January 1, 2011.

Net Investment Income. Investment portfolio yield decreased approximately 92 basis points at March 31, 2011 compared to the same period in 2010 due to the prevailing low interest rate environment.

Net investment income performance is summarized as follows.

| | Three | Year Ended | Three Months |
|---|-------------------------------------|---------------------|---------------------|
| | Months | December 31, | Ended |
| | Ended | 2010 | March 31, |
| | March 31, | | 2010 |
| | 2011 | | |
| | (In thousands, except for %) | | |
| Net investment income, annualized | \$ 30,056 | 30,077 | 33,396 |
| Average invested assets, at amortized cost | \$ 740,549 | 696,134 | 671,389 |
| Annualized yield on average invested assets | 4.06% | 4.32% | 4.97% |

We have traditionally invested in fixed maturity securities with a large percent held in callable issues. We 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, and is reflected in 2011 investment results.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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Investment income from debt securities accounted for approximately 86.0% of total investment income for the three months ended March 31, 2011. We continue to hold investments in bonds of U.S. Government-sponsored enterprises, such as FNMA and FHLMC, which comprised 55.1% of the total fixed maturity portfolio based on amortized cost at March 31, 2011. We have increased our investment purchases of corporate and municipal securities over the past several quarters, focusing on utility service sectors in the corporate securities.

| | Three Months Ended | |
|---------------------------|---------------------------|-------------|
| | March 31, | |
| | 2011 | 2010 |
| | (In thousands) | |
| Gross investment income: | | |
| Fixed maturity securities | \$ 6,517 | 7,386 |
| Equity securities | 197 | 149 |
| Mortgage loans | 27 | 18 |
| Policy loans | 710 | 656 |
| Long-term investments | 53 | 68 |
| Other investment income | 75 | 197 |
| | | |
| Total investment income | 7,579 | 8,474 |
| Investment expenses | (65) | (125) |
| | | |
| Net investment income | \$ 7,514 | 8,349 |

The increased call activity of bonds in our portfolio combined with lower yields on reinvested assets is likely to result in lower investment income going forward despite higher levels of invested assets unless interest rates increase. The decrease in fixed maturity securities investment income in 2011 resulted from the declining yields as previously noted. The increase in the asset balance of policy loans, which represents policyholders utilizing their accumulated policy cash value, has resulted in a correlating increase to investment income.

Realized Gains (Losses), Net. The Company recorded a valuation allowance of \$45,000 during the first quarter of 2010 on a non-performing mortgage loan.

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.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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Benefits and Expenses

| | Three Months Ended March 31, | |
|---|---|---------------|
| | 2011 | 2010 |
| | (In thousands) | |
| Benefits and expenses: | | |
| Insurance benefits paid or provided: | | |
| Claims and surrenders | \$ 14,879 | 15,577 |
| Increase in future policy benefit reserves | 12,318 | 9,545 |
| Policyholders dividends | 1,662 | 1,570 |
| Total insurance benefits paid or provided | 28,859 | 26,692 |
| Commissions | 9,072 | 8,128 |
| Other underwriting, acquisition and insurance expenses | 6,610 | 6,853 |
| Capitalization of deferred policy acquisition costs | (7,165) | (5,995) |
| Amortization of deferred policy acquisition costs | 4,520 | 4,944 |
| Amortization of cost of customer relationships acquired and other intangibles | 654 | 838 |
| Total benefits and expenses | \$ 42,550 | 41,460 |

A detail of claim and surrender benefits is provided below.

| | Three Months Ended March 31, | |
|------------------------------------|---|---------------|
| | 2011 | 2010 |
| | (In thousands) | |
| Death claims | \$ 6,026 | 6,135 |
| Surrender benefits | 4,362 | 4,894 |
| Endowment benefits | 3,401 | 3,291 |
| Property claims | 553 | 564 |
| Accident and health benefits | 105 | 260 |
| Other policy benefits | 432 | 433 |
| Total claims and surrenders | \$ 14,879 | 15,577 |

Increase in Future Policy Benefit Reserves. Reserves as of March 31, 2011 reflect a change in product sales internationally to endowments that produce a faster reserve build up than whole life products. The current period of 2011 includes a reserve decrease of \$0.2 million related to an adjustment in reserve calculation of certain SPLIC policies. In addition, a reserve decrease of \$0.1 million was recorded as certain reserve estimates were refined in the current period related to the home service segment.

Policyholder Dividends. Policyholder dividends increased during the three months ended March 31, 2011 compared to the same period in 2010, 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

premium rates charged. 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 increased from the prior year amounts as premium revenues increased.

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Other Underwriting, Acquisition and Insurance Expenses. The decrease in these expenses related to salaries and legal expenses in the current year compared to the same period in 2010. The decline in salary expense is reflective of staff reductions that occurred related to operating efficiencies from previous acquisitions. The legal expense in 2010 included fees related to a CNLIC claim settlement of \$0.2 million, which was a one-time event increasing reported expenses for that year.

Capitalized Deferred Policy Acquisition Costs. Costs capitalized under current accounting guidance include certain commissions, policy issuance costs, underwriting and agency expenses that relate to and vary with the production of new business.

Amortization of Deferred Policy Acquisition Costs. Amortization decreased for the three months ended March 31, 2011 compared to the same period in 2010 due to an adjustment of \$0.3 million that decreased amortization in the current period, which related to a refinement of estimates utilizing system generated information. Overall, the Company has experienced improved persistency compared to the same period in 2010 that would also result in decreasing amortization.

Federal Income Tax. The effective tax rate for the three months ended March 31, 2011 was 34.9% versus 32.3% for the same periods in 2010. 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.

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.

| | Income (Loss) Before Income Taxes | |
|---------------------------------|--|--------------|
| | Three Months Ended March 31, | |
| | 2011 | 2010 |
| | (In thousands) | |
| Life Insurance | \$ 905 | 1,618 |
| Home Service Insurance | 1,779 | 1,020 |
| Other Non-Insurance Enterprises | 49 | (266) |
| Total | \$ 2,733 | 2,372 |

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**CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011**

Life Insurance

Our Life Insurance segment consists of issuing ordinary whole life insurance domestically and in U.S. Dollar-denominated amounts to foreign residents. These contracts are designed to provide a fixed amount of insurance coverage over the life of the insured. Additionally, endowment contracts are issued by the Company, which are principally accumulation contracts that incorporate an element of life insurance protection. For the majority of our business, we retain only the first \$100,000 of risk on any one life. We operate this segment through our subsidiaries: CICA Life Insurance Company of America (CICA), Citizens National Life Insurance Company, (CNLIC) and Integrity Capital Insurance Company (ICIC).

International Sales

We focus our sales of U.S. Dollar-denominated ordinary whole life insurance and endowment policies to high net worth, high income residents in Latin America and the Pacific Rim. We have successfully participated in the foreign marketplace since 1975, and we continue to seek opportunities for expansion of our foreign operations. We believe positive attributes of our international insurance business include:

- larger face amount policies typically issued when compared to our U.S. operations, which results in lower underwriting and administrative costs per unit of coverage;
- premiums are typically paid annually rather than monthly or quarterly, which saves us administrative expenses, accelerates cash flow and results in lower policy lapse rates than premiums with more frequently scheduled payments;
- favorable persistency levels and mortality rates comparable to our U.S. policies.

International Products

We offer several ordinary whole life insurance and endowment products designed to meet the needs of our non-U.S. policy owners. These policies have been structured to provide:

- U.S. Dollar-denominated cash values that accumulate, beginning in the first policy year, to a policyholder during his or her lifetime;
- premium rates that are competitive with or better than most foreign local companies;
- a hedge against local currency inflation;
- protection against devaluation of foreign currency;
- capital investment in a more secure economic environment (i.e., the United States); and
- lifetime income guarantees for an insured or for surviving beneficiaries.

Our international products have living benefit features. Every policy contains guaranteed cash values and is participating (i.e., provides for cash dividends as apportioned by the board of directors). Once a policy owner pays the annual premium and the policy is issued, we immediately pay a cash dividend as well as an annual guaranteed endowment, if elected, to the owner. The policy owner has several options with regard to the dividend, including the right to assign dividends to our stock investment plan, registered under the Securities Act of 1933 (the Securities Act), and administered in the United States by our unaffiliated transfer agent.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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The following table sets forth, by territory, our total percentages of direct collected premiums from our international life insurance business for the periods indicated. The information is presented in accordance with statutory accounting practices prescribed by the state of Colorado, the state of domicile of CICA, our subsidiary that writes all of our international business.

| Country | Three Months Ended March 31, | | | |
|----------------|-------------------------------------|---------------|------------------|---------------|
| | 2011 | | 2010 | |
| | (In thousands) | | | |
| Colombia | \$ 5,022 | 19.6% | \$ 5,057 | 21.6% |
| Venezuela | 4,596 | 17.9 | 3,442 | 14.7 |
| Taiwan | 4,448 | 17.4 | 4,194 | 17.9 |
| Ecuador | 3,029 | 11.8 | 2,799 | 11.9 |
| Argentina | 1,886 | 7.4 | 1,848 | 7.9 |
| Other Non-U.S. | 6,643 | 25.9 | 6,080 | 26.0 |
| Total | \$ 25,624 | 100.0% | \$ 23,420 | 100.0% |

Domestic Sales

In the midwest and the southern United States, we seek to serve middle income households through the sale of cash accumulation ordinary whole life insurance products. The majority of our inforce business results from blocks of business of insurance companies we have acquired over the past 15 years.

Domestic Products

Our domestic life insurance products focus primarily on living needs and provide benefits focused toward accumulating money for living benefits while providing a modest death benefit for the policyowner. The features of our domestic life insurance products include:

- cash accumulation/living benefits;
- tax-deferred interest earnings;
- guaranteed lifetime income or monthly income options for the policyowner or surviving family members;
- accidental death benefit coverage options; and
- an option to waive premium payments in the event of disability.

Our life insurance products are principally designed to address the insured's concern about outliving his or her monthly income, while at the same time providing death benefits. The primary purpose of our product portfolio is to help the insured create capital for needs such as retirement income, children's higher education funds, business opportunities, emergencies and health care needs.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
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The following table sets forth our direct collected life insurance premiums by state for the periods indicated, in accordance with statutory accounting practices prescribed by the states of domicile of our insurance company subsidiaries.

| State | Three Months Ended March 31, | | | |
|--------------|-------------------------------------|---------------|-----------------|---------------|
| | 2011 | | 2010 | |
| | (In thousands) | | | |
| Texas | \$ 1,293 | 35.6% | \$ 1,565 | 36.9% |
| Indiana | 503 | 13.8 | 535 | 12.6 |
| Missouri | 388 | 10.7 | 435 | 10.3 |
| Kentucky | 335 | 9.2 | 413 | 9.8 |
| Mississippi | 282 | 7.7 | 334 | 7.9 |
| Other States | 839 | 23.0 | 953 | 22.5 |
| Total | \$ 3,640 | 100.0% | \$ 4,235 | 100.0% |

A number of domestic life insurance companies we acquired had blocks of accident and health insurance policies, which we did not consider to be a core part of our business. We have ceded this business under a coinsurance agreement with an unaffiliated insurance company under which it assumes substantially all of our accident and health policies. The premium amounts ceded under the coinsurance agreement for the three months ended March 31, 2011 and 2010 were \$1.2 million and \$1.4 million, respectively.

The results of operations for the life segment for the periods indicated are as follows.

| | Three Months Ended March | |
|--|---------------------------------|---------------|
| | 31, | |
| | 2011 | 2010 |
| | (In thousands) | |
| Revenue: | | |
| Premiums | \$ 26,520 | 24,769 |
| Net investment income | 4,081 | 4,711 |
| Realized gains (losses), net | | (29) |
| Other income | 87 | 277 |
| Total revenue | 30,688 | 29,728 |
| Benefits and expenses: | | |
| Insurance benefits paid or provided: | | |
| Claims and surrenders | 9,401 | 9,899 |
| Increase in future policy benefit reserves | 11,809 | 8,662 |
| Policyholders dividends | 1,643 | 1,542 |
| Total insurance benefits paid or provided | 22,853 | 20,103 |
| Commissions | 5,342 | 4,505 |
| Other underwriting, acquisition and insurance expenses | 2,954 | 2,977 |
| Capitalization of deferred policy acquisition costs | (5,427) | (4,464) |

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| | | |
|--|--------|--------|
| Amortization of deferred policy acquisition costs | 3,838 | 4,659 |
| Amortization of cost of customer relationship acquired and other intangibles | 223 | 330 |
| Total benefits and expenses | 29,783 | 28,110 |
| Income before income tax expense | \$ 905 | 1,618 |

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Premiums. Premium revenues increased for the three months ended March 31, 2011 compared to the same three months in 2010 due primarily to international business, which experienced good persistency as this block of insurance matures. First year premiums increased 28% for the current period ended in 2011 compared to the same period in 2010. Renewals accounted for approximately 87% and 85% of total premium for the three months ended in 2010 and 2011, respectively.

Life Insurance premium breakout is detailed below.

| | Three Months Ended March 31, | |
|--------------------|-------------------------------------|---------------|
| | 2011 | 2010 |
| | (In thousands) | |
| Premiums: | | |
| First year | \$ 4,098 | \$ 3,212 |
| Renewal | 22,422 | 21,557 |
| Total premiums | \$ 26,520 | \$ 24,769 |

Net Investment Income. Net investment income decreased comparing the three months ended March 31, 2011 to the same period of 2010 due to the declining interest rate environment and the significant call activity the Company experienced related to fixed income debt securities during 2009 and 2010. These proceeds were reinvested into lower yielding securities, thus decreasing the yield rate by approximately 112 basis points.

| | Three Months Ended March 31, 2011 | Year Ended December 31, 2010 | Three Months Ended March 31, 2010 |
|---|--|-------------------------------------|--|
| | (In thousands, except for %) | | |
| Net investment income, annualized | \$ 16,324 | 16,523 | 18,844 |
| Average invested assets, at amortized cost | \$ 424,226 | 396,360 | 379,217 |
| Annualized yield on average invested assets | 3.85% | 4.17% | 4.97% |

Claims and Surrenders. Claims and surrenders decreased for the three months ended March 31, 2011 compared to the same period in 2010. These amounts fluctuate from period to period but were within anticipated ranges based upon management's expectations.

| | Three Months Ended March 31, | |
|------------------------------|-------------------------------------|-------------|
| | 2011 | 2010 |
| | (In thousands) | |
| Death claims | \$ 1,848 | 1,743 |
| Surrender benefits | 3,746 | 4,363 |
| Endowment benefits | 3,395 | 3,284 |
| Accident and health benefits | 71 | 194 |
| Other policy benefits | 341 | 315 |

| | | | |
|-----------------------------|----|-------|-------|
| Total claims and surrenders | \$ | 9,401 | 9,899 |
|-----------------------------|----|-------|-------|

Surrender benefits decreased for the three months ended March 31, 2011 compared to the same period in 2010. Surrenders as a percent of ordinary whole life insurance in force decreased from 0.4% at December 31, 2010 to 0.3% in the first three months of 2011. The majority of policy surrender benefits paid is attributable to our international business and was related to policies that have been in force over fifteen years, where surrender charges are no longer applicable.

Endowment benefit expense has increased due to the election by policyholders of a product feature that provides an annual benefit. This is a fixed benefit over the life of the contract and as persistency improves this expense will increase.

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Increase in Future Policy Benefit Reserves. Policy benefit reserves increased for the three months ended March 31, 2011 compared to the same period in 2010, 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 75% and 63% of total in force for new policies issued through the three months in 2011 and 2010, respectively.

Commissions. Commission expense increased for the three months ended March 31, 2011 compared to the same period in 2010, as premium revenues increased. This expense fluctuates directly with premium revenues.

Amortization of Deferred Policy Acquisition Costs (DAC). Amortization costs decreased for the three months ended March 31, 2011 compared to 2010 resulting from improved persistency. The Company canceled its contract with a newly-recruited high volume producer in the second quarter of 2009 due to poor experience, and policies sold by this organization lapsed at high rates during the first and second quarter of 2010, which resulted in higher DAC amortization in those periods.

Home Service Insurance

We operate in the Home Service market through our subsidiaries Security Plan Life Insurance Company (SPLIC) and Security Plan Fire Insurance Company (SPFIC), and focus on the life insurance needs of the middle and lower income markets, primarily in Louisiana, Mississippi and Arkansas. Our policies are sold and serviced through a home service marketing distribution system of approximately 330 employee-agents who work full time on a route system and through funeral homes to sell policies, collect premiums and service policyholders.

The following table sets forth our direct collected life insurance premiums by state for the periods indicated, in accordance with statutory accounting practices prescribed by the states of domicile of our insurance company subsidiaries.

| State | Three Months Ended March 31, | | | |
|--------------|-------------------------------------|---------------|------------------|---------------|
| | 2011 | | 2010 | |
| | (In thousands) | | | |
| Louisiana | \$ 10,198 | 88.2% | \$ 9,970 | 87.5% |
| Arkansas | 1,017 | 8.8 | 1,059 | 9.3 |
| Mississippi | 91 | 0.8 | 85 | 0.7 |
| Other States | 257 | 2.2 | 283 | 2.5 |
| Total | \$ 11,563 | 100.0% | \$ 11,397 | 100.0% |

Home Service Products

Our home service insurance products consist primarily of small face amount ordinary whole life and pre-need policies, which are designed to fund final expenses for the insured, primarily consisting of funeral and burial costs. To a much lesser extent, our Home Service Insurance segment sells limited-liability, named-peril property policies covering dwellings and contents. We provide \$30,000 maximum coverage on any one dwelling and contents, while content only coverage and dwelling only coverage is limited to \$20,000.

We provide final expense ordinary life insurance and annuity products primarily to middle and lower income individuals in Louisiana, Mississippi and Arkansas.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

The results of operations for the home service segment for the periods indicated are as follows.

| | Three Months Ended March 31, | |
|--|---|---------------|
| | 2011 | 2010 |
| | (In thousands) | |
| Revenue: | | |
| Premiums | \$ 10,708 | 10,421 |
| Net investment income | 3,237 | 3,532 |
| Realized gains (losses), net | 19 | 133 |
| Other income | 8 | 49 |
| Total revenue | 13,972 | 14,135 |
| Benefits and expenses: | | |
| Insurance benefits paid or provided: | | |
| Claims and surrenders | 5,478 | 5,678 |
| Increase in future policy benefit reserves | 509 | 883 |
| Policyholders dividends | 19 | 28 |
| Total insurance benefits paid or provided | 6,006 | 6,589 |
| Commissions | 3,730 | 3,623 |
| Other underwriting, acquisition and insurance expenses | 3,082 | 3,641 |
| Capitalization of deferred policy acquisition costs | (1,738) | (1,531) |
| Amortization of deferred policy acquisition costs | 682 | 285 |
| Amortization of cost of customer relationship acquired and other intangibles | 431 | 508 |
| Total benefits and expenses | 12,193 | 13,115 |
| Income before income tax expense | \$ 1,779 | 1,020 |

Premiums. The premium increases were due to enhanced marketing efforts to promote the Home Service segment, as well as a SPFIC rate increase of 5.7% that became effective January 1, 2011.

Net Investment Income. Net investment income decreased for the three months ended March 31, 2011 compared to the same periods in 2010 as the Company experienced significant call activity in 2009 and 2010 with reinvestment during a declining interest rate environment, which depressed our investment income and has lowered portfolio yields by 57 basis points.

| Three Months Ended March 31, 2011 | Year Ended December 31, 2010 | Three Months Ended March 31, 2010 |
|--|---|--|
| (In thousands, except for %) | | |

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| | | | |
|---|------------|---------|---------|
| Net investment income, annualized | \$ 12,948 | 13,008 | 14,128 |
| Average invested assets, at amortized cost | \$ 284,171 | 279,682 | 275,421 |
| Annualized yield on average invested assets | 4.56% | 4.65% | 5.13% |

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Realized Gains, Net. Realized gains in the first quarter of 2010 resulted from the sale of one bond in SPLIC's portfolio.
Claims and Surrenders. Claims and surrenders decreased for the three month period ended March 31, 2011 compared to the same period in 2010.

| | For the Three Months Ended March | |
|------------------------------------|---|--------------|
| | 31, | |
| | 2011 | 2010 |
| | (In thousands) | |
| Death claims | \$ 4,178 | 4,392 |
| Surrender benefits | 616 | 531 |
| Endowment benefits | 6 | 7 |
| Property claims | 553 | 564 |
| Accident and health benefits | 34 | 66 |
| Other policy benefits | 91 | 118 |
| Total claims and surrenders | \$ 5,478 | 5,678 |

Death claims decreased 4.9% for the three months ended March 31, 2011 compared to the same period in 2010. Mortality experience is closely monitored by the Company as a key performance indicator and these amounts were within expected levels.

Surrender benefits have increased in the three months ended March 31, 2011 compared to the same period in 2010, which is consistent with a growing block of business.

Other Underwriting, Acquisition and Insurance Expenses. Other underwriting, acquisition and insurance expenses decreased for the three months ended March 31, 2011 compared to the same period in 2010, due to an overall decrease in expenses and a reallocation of expenses that became effective January 1, 2011 that reduced the home service segment and increased the life segment allocation in the current year.

Amortization of Deferred Policy Acquisition Costs. Amortization increased in the current period of 2011 by \$0.3 million due to a refinement in an estimate using system generated information related to SPLIC assumptions.

Other Non-Insurance Enterprises

Overall, other non-insurance operations are relatively immaterial to the consolidated results, except for the fair value adjustment related to the Company's warrants to purchase Class A common stock. These amounts fluctuate due to the movement in the stock price and fair value calculation using the Black-Scholes valuation model.

Investments

The administration of our investment portfolios is handled by our management, pursuant to board-approved investment guidelines, with all trading activity approved by a committee of the respective boards of directors of our insurance company subsidiaries. The guidelines used require that fixed maturities, both government and corporate, are of high quality and comprise a majority of the investment portfolio. State insurance statutes prescribe the quality and percentage of the various types of investments that may be made by insurance companies and generally permit investment in qualified state, municipal, federal and foreign government obligations, high quality corporate bonds, preferred and common stock, mortgage loans and real estate within certain specified percentages. The assets are intended to mature in accordance with the average maturity of the insurance products and to provide the cash flow for our insurance company subsidiaries to meet their respective policyholder obligations.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

The following table shows the carrying value of our investments by investment category and cash and cash equivalents, and the percentage of each to total invested assets.

| | March 31, 2011 | | December 31, 2010 | |
|---|-----------------------|-------------------|--------------------------|-------------------|
| | Carrying | % of Total | Carrying | % of Total |
| | Value | Carrying | Value | Carrying |
| | (In | Value | (In | Value |
| | thousands) | | thousands) | |
| Fixed maturity securities: | | | | |
| U.S. Treasury and U.S. Government-sponsored enterprises | \$ 385,567 | 48.4% | \$ 378,012 | 48.8% |
| Mortgage-backed (1) | 13,415 | 1.7 | 14,808 | 1.9 |
| Municipal bonds | 123,728 | 15.5 | 101,719 | 13.1 |
| Corporate | 164,852 | 20.7 | 161,298 | 20.8 |
| Foreign governments | 130 | | 132 | |
| Total fixed maturity securities | 687,692 | 86.3 | 655,969 | 84.6 |
| Cash and cash equivalents | 37,450 | 4.7 | 49,723 | 6.4 |
| Other investments: | | | | |
| Policy loans | 36,306 | 4.6 | 35,585 | 4.6 |
| Equity securities | 23,815 | 3.0 | 23,304 | 3.0 |
| Mortgage loans | 1,478 | 0.2 | 1,489 | 0.2 |
| Real estate and other long-term investments | 9,314 | 1.2 | 9,348 | 1.2 |
| Total cash, cash equivalents and investments | \$ 796,055 | 100.0% | \$ 775,418 | 100.0% |

(1) Includes \$12.5 million and \$13.2 million of U.S. Government-sponsored enterprises at March 31, 2011 and December, 2010, respectively.

The Company increased holdings in municipal and corporate securities, investing in shorter duration investment grade securities and in municipal securities with higher yields during the first three months of 2011. Cash and cash equivalents decreased as of March 31, 2011 due to purchased investments of fixed maturity securities that occurred during the current quarter.

The held-to-maturity portfolio as of March 31, 2011 represented 9.8% of the total fixed maturity securities owned based upon carrying values, with the remaining 90.2% classified as available-for-sale. Held-to-maturity securities are reported in the financial statements at amortized cost and available-for-sale securities are reported at fair value.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

The following table sets forth the distribution of the credit ratings of our portfolio of fixed maturity securities by carrying value as of March 31, 2011 and December 31, 2010.

| | March 31, 2011 | | December 31, 2010 | |
|-------------------------|--|----------|--|----------|
| | Carrying Value (In thousands) | % | Carrying Value (In thousands) | % |
| AAA and U.S. Government | \$ 420,094 | 61.1% | \$ 428,194 | 65.3% |
| AA | 97,840 | 14.2 | 59,454 | 9.1 |
| A | 73,274 | 10.7 | 73,341 | 11.2 |
| BBB | 84,861 | 12.3 | 84,489 | 12.9 |
| BB and other | 11,623 | 1.7 | 10,491 | 1.5 |
| Totals | \$ 687,692 | 100.0% | \$ 655,969 | 100.0% |

The increase in fixed maturities with credit ratings of AA as of March 31, 2011 compared to December 31, 2010 is a result of new investments in taxable municipals and corporate bonds, primarily public utility issuers with an average maturity of seven years. The increase in non-investment grade securities was due to down-grades of issuers in the current period, as the Company does not purchase below investment grade securities.

Valuation of Investments

We evaluate the carrying value of our fixed maturity and equity securities at least quarterly. 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 did not recognize any other-than-temporary impairments during the three months ended March 31, 2011 or March 31, 2010. The Company recognized a valuation allowance on one mortgage loan totaling \$45,000 during the first quarter of 2010.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Liquidity and Capital Resources

Liquidity refers to a company's ability to generate sufficient cash flows to meet the needs of its operations. Liquidity is managed on insurance operations and seeks to ensure stable and reliable sources of cash flows to meet obligations provided by a variety of sources.

Liquidity requirements of Citizens are met primarily by funds provided from operations. Premium deposits and revenues, investment income and investment maturities are the primary sources of funds, while investment purchases, policy benefits, and operating expenses are the primary uses of funds. We historically have not had to liquidate investments to provide cash flow and did not do so during the first three months of 2011. Our investments as of March 31, 2011 consist of 81.8% of marketable debt securities classified as available-for-sale that could be readily converted to cash for liquidity needs.

A primary liquidity concern is the risk of an extraordinary level of early policyholder withdrawals. We include provisions within our insurance policies, such as surrender charges, that help limit and discourage early withdrawals. Since these contractual withdrawals, as well as the level of surrenders experienced, were largely consistent with our assumptions in asset liability management, our associated cash outflows have, to date, not had an adverse impact on our overall liquidity. Individual life insurance policies are less susceptible to withdrawal than annuity reserves and deposit liabilities because policyholders may incur surrender charges and undergo a new underwriting process in order to obtain a new insurance policy. Cash flow projections and cash flow tests under various market interest rate scenarios are also performed annually to assist in evaluating liquidity needs and adequacy. We currently anticipate that available liquidity sources and future cash flows will be adequate to meet our needs for funds.

Cash flows from our insurance operations have been sufficient to meet current needs. Cash flows from operating activities were \$14.3 million and \$12.6 million for the three months ended March 31, 2011 and 2010, respectively. We have traditionally also had significant cash flows from both scheduled and unscheduled investment security maturities, redemptions, and prepayments. These cash flows, for the most part, are reinvested in fixed income securities. Net cash outflows from investment activity totaled \$27.2 million and \$13.6 million for the three months ended March 31, 2011 and 2010, respectively.

The National Association of Insurance Commissioners (NAIC) has established minimum capital requirements in the form of Risk-Based Capital (RBC). Risk-based capital factors the type of business written by an insurance company, the quality of its assets, and various other aspects of an insurance company's business to develop a minimum level of capital called "authorized control level risk-based capital" and compares this level to adjusted statutory capital that includes capital and surplus as reported under statutory accounting principles, plus certain investment reserves. Should the ratio of adjusted statutory capital to control level risk-based capital fall below 200%, a series of actions by the affected company would begin.

All insurance subsidiaries were above the RBC minimums at March 31, 2011 and did not change significantly from levels at December 31, 2010. The ratio of adjusted statutory capital to control level risk-based capital is shown below.

| | March 31, 2011 |
|-------|---------------------------|
| CICA | 890% |
| SPLIC | 1,270% |
| CNLIC | 2,754% |
| SPFIC | 324% |
| ICIC | 4,373% |

Contractual Obligations and Off-balance Sheet Arrangements

There have been no material changes in contractual obligations from those reported in the Company's Form 10-K for the year ended December 31, 2010. The Company does not have off-balance sheet arrangements at March 31, 2011 and does not expect any future effects on the Company's financial condition related to any such arrangements. We do

not utilize special purpose entities as investment vehicles, nor are there any such entities in which we have an investment that engages in speculative activities of any nature, and we do not use such investments to hedge our investment positions.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Parent Company Liquidity and Capital Resources

We are a holding company and have had minimal operations of our own. Our assets consist primarily of the capital stock of our subsidiaries, cash and investment real estate. Accordingly, our cash flows depend upon the availability of statutorily permissible payments, primarily payments under management agreements from our two primary life insurance subsidiaries, CICA and SPLIC. The ability to make payments is limited by applicable laws and regulations of Colorado, CICA's state of domicile, and Louisiana, SPLIC's state of domicile, which subject insurance operations to significant regulatory restrictions. These laws and regulations require, among other things, that these insurance subsidiaries maintain minimum solvency requirements and limit the amount of dividends these subsidiaries can pay to the holding company. We historically have not relied upon dividends from subsidiaries for our cash flow needs.

Critical Accounting Policies

Our critical accounting policies are as follows:

Policy Liabilities

Future policy benefit reserves have been computed by the net level premium method with assumptions as to investment yields, dividends on participating business, mortality and withdrawals based upon our experience. The preparation of financial statements requires management to make estimates and assumptions that affect the reported amount of policy liabilities and the increase in future policy benefit reserves. Management's judgments and estimates for future policy benefit reserves provide for possible unfavorable deviation.

We continue to use the original assumptions (including a provision for the risk of adverse deviation) in subsequent periods to determine the changes in the liability for future policy benefits (the "lock-in" concept) unless a premium deficiency exists. Management monitors these assumptions and has determined that a premium deficiency did not exist as of March 31, 2011. Management believes that our policy liabilities and increase in future policy benefit reserves as of the three months ended March 31, 2011 and 2010 are based upon assumptions, including a provision for the risk of adverse deviation, that do not warrant revision.

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.

Deferred Policy Acquisition Costs

Acquisition costs, consisting of commissions and policy issuance, underwriting and agency expenses that relate to and vary with the production of new business, are deferred. These deferred policy acquisition costs are amortized primarily over the estimated premium paying period of the related policies in proportion to the ratio of the annual premium recognized to the total premium revenue anticipated, using the same assumptions as were used in computing liabilities for future policy benefits.

We utilize the factor method to determine the amount of costs to be capitalized and the ending asset balance. The factor method is based on the ratio of premium revenue recognized for the policies in force at the end of each reporting period compared to the premium revenue recognized for policies in force at the beginning of the reporting period. The factor method ensures that policies that lapsed or surrendered during the reporting period are no longer included in the deferred policy acquisition costs calculation. The factor method limits the amount of deferred costs to its estimated realizable value, provided actual experience is comparable to that contemplated in the factors.

Inherent in the capitalization and amortization of deferred policy acquisition costs are certain management judgments about what acquisition costs are deferred, the ending asset balance and the annual amortization. Approximately 80% of our capitalized deferred acquisition costs are attributed to first year excess commissions. The remaining 20% are attributed to costs that vary with and are directly related to the acquisition of new insurance business. Those costs generally include costs related to the production, underwriting and issuance of new business.

Table of Contents**CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES****March 31, 2011**

A recoverability test that considers, among other things, actual experience and projected future experience is performed at least annually. These annual recoverability tests initially calculate the available premium (gross premium less benefit and expense portion of premium) for the next 30 years. The available premium per policy and the deferred policy acquisition costs per policy are then calculated. The deferred policy acquisition costs are then evaluated over two methods utilizing reasonable assumptions and two other methods using pessimistic assumptions. The two methods using reasonable assumptions illustrate an early-deferred policy acquisition recoverability period. The two methods utilizing pessimistic assumptions still support early recoverability of our aggregate deferred policy acquisition costs. Management believes that our deferred policy acquisition costs and related amortization for the three months ended March 31, 2011 and 2010 limits the amount of deferred costs to its estimated realizable value. This belief is based upon the analysis performed on capitalized expenses that vary with and are primarily related to the acquisition of new and renewal insurance business, utilization of the factor method and annual recoverability testing.

Cost of Customer Relationships Acquired

Cost of Customer Relationships Acquired (CCRA) is established when we purchase a block of insurance. CCRA is amortized primarily over the emerging profit of the related policies using the same assumptions as were used in computing liabilities for future policy benefits. We utilize various methods to determine the amount of the ending asset balance, including a static model and a dynamic model. Inherent in the amortization of CCRA are certain management judgments about the ending asset balance and the annual amortization. The assumptions used are based upon interest, mortality and lapses at the time of purchase.

A recoverability test that considers, among other things, actual experience and projected future experience is performed at least annually. These annual recoverability tests initially calculate the available premium (gross premium less benefit and expense portion of premium) for the next thirty years. The CCRA is then evaluated utilizing reasonable assumptions. Management believes that our CCRA and related amortization is recoverable for the three months ended March 31, 2011 and 2010. This belief is based upon the analysis performed on estimated future results of the block and our annual recoverability testing.

Goodwill

Current accounting guidance requires that goodwill balances be reviewed for impairment at least annually or more frequently if events occur or circumstances change that would indicate that a triggering event has occurred. A reporting unit is defined as an operating segment on one level below an operating segment. Most of the Company's reporting units, for which goodwill has been allocated, are equivalent to the Company's operating segment, as there is no discrete financial information available for the separate components of the segment or all of the components of the segment have similar economic characteristics.

The goodwill impairment test follows a two step process as defined under current accounting guidance. In the first step, the fair value of a reporting unit is compared to its carrying value. If the carrying value of a reporting unit exceeds its fair value, the second step of the impairment test is performed for purposes of measuring the impairment. In the second step, the fair value of the reporting unit is allocated to all of the assets and liabilities of the reporting unit to determine an implied goodwill value. If the carrying amount of the reporting unit goodwill exceeds the implied goodwill value, an impairment loss is recognized in an amount equal to that excess.

Management's determination of the fair value of each reporting unit incorporates multiple inputs including discounted cash flow calculations, peer company price to earnings multiples, the level of the Company's Class A common stock price and assumptions that market participants would make in valuing the reporting unit. Other assumptions can include levels of economic capital, future business growth, and earnings projections.

Valuation of Investments in Fixed Maturity and Equity Securities

The evaluation of securities for impairments is a quantitative and qualitative process, which is subject to risks and uncertainties and is intended to determine whether declines in the fair value of investments should be recognized in current period earnings. The risks and uncertainties include changes in general economic conditions, the issuer's financial condition or future prospects, the effects of changes in interest rates or credit spreads and the expected recovery period.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Based upon current accounting guidance, investment securities must be classified as held-to-maturity, available-for-sale or trading. Management determines the appropriate classification at the time of purchase. The classification of securities is significant since it directly impacts the accounting for unrealized gains and losses on securities. Fixed maturity securities are classified as held-to-maturity and carried at amortized cost when management has the positive intent and the Company has the ability to hold the securities to maturity. Securities not classified as held-to-maturity are classified as available-for-sale and are carried at fair value, with the unrealized holding gains and losses, net of tax, reported in other comprehensive income and do not affect earnings until realized.

The Company evaluates all securities on a quarterly basis, and more frequently when economic conditions warrant additional evaluations, for determining if an OTTI exists pursuant to the accounting guidelines. In evaluating the possible impairment of securities, consideration is given to the length of time and the extent to which the fair value has been less than cost, the financial conditions and near-term prospects of the issuer, and the ability and intent of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. In analyzing an issuer's financial condition, the Company may consider whether the securities are issued by the Federal government or its agencies, by government-sponsored agencies, or whether downgrades by bond rating agencies have occurred, and reviews of the issuer's financial condition.

If management determines an investment has experienced an OTTI, management must then determine the amount of OTTI to be recognized in earnings. If management does not intend to sell the security and it is more likely than not that the Company will not be required to sell the security before recovery of its amortized cost basis less any current period loss, the OTTI will be separated into the amount representing the credit loss and the amount related to all other factors. The amount of OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized in earnings. The amount of OTTI related to other factors will be recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings will become the new amortized cost basis of the investment. If management intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current period credit loss, the OTTI will be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. The new amortized cost basis is not adjusted for subsequent recoveries in fair value.

The Company from time to time may dispose of an impaired security in response to asset/liability management decisions, future market movements, business plan changes, or if the net proceeds can be reinvested at a rate of return that is expected to recover the loss within a reasonable period of time.

Premium Revenue and Related Expenses

Premiums on life and accident and health policies are reported as earned when due or, for short duration contracts, over the contract period on a pro rata basis. Benefits and expenses are associated with earned premiums so as to result in recognition of profits over the estimated life of the contracts. This matching is accomplished by means of provisions for future benefits and the capitalization and amortization of deferred policy acquisition costs.

Annuities are accounted for in a manner consistent with accounting for interest bearing financial instruments. Our most popular annuity products do not include fees or other such charges.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK*General*

The nature of our business exposes us to investment market risk. Market risk is the risk of loss that may occur when changes in interest rates and public equity prices adversely affect the value of our invested assets. Interest rate risk is our primary market risk exposure. Substantial and sustained increases and decreases in market interest rates can affect the fair value of our investments. The fair value of our fixed maturity portfolio generally increases when interest rates decrease and decreases when interest rates increase.

The following table summarizes net unrealized gains and losses for the periods indicated.

| | March 31, 2011 | | Net Unrealized Gains (Losses) (In thousands) | December 31, 2010 | | Net Unrealized Gains (Losses) |
|---|-------------------|---------------|--|-------------------|---------------|--|
| | Amortized Cost | Fair Value | | Amortized Cost | Fair Value | |
| Fixed maturities, available-for-sale | \$ 622,282 | 620,614 | (1,668) | 578,412 | 575,737 | (2,675) |
| Fixed maturities, held-to-maturity | 67,078 | 65,611 | (1,467) | 80,232 | 79,103 | (1,129) |
| Total fixed maturities | \$ 689,360 | 686,225 | (3,135) | 658,644 | 654,840 | (3,804) |
| Total equity securities | \$ 19,729 | 23,815 | 4,086 | 19,844 | 23,304 | 3,460 |

Market Risk Related to Interest Rates

Our exposure to interest rate changes results from our significant holdings of fixed maturity investments, which comprised 91% of our investment portfolio as of March 31, 2011. These investments are mainly exposed to changes in U.S. Treasury rates. Our fixed maturities investments include U.S. Government-sponsored enterprises, U.S. Government bonds, securities issued by government agencies, and corporate bonds. Approximately 54.2% of the fixed maturities at fair value as of March 31, 2011 were invested in U.S. Government-sponsored enterprises, or were backed by U.S. Government agencies.

To manage interest rate risk, we perform periodic projections of asset and liability cash flows to evaluate the potential sensitivity of our investments and liabilities. We assess interest rate sensitivity with respect to our available-for-sale fixed maturities investments using hypothetical test scenarios that assume either upward or downward shifts in the prevailing interest rates. The change in fair values of our debt and equity securities as of March 31, 2011 were within the expected range of this analysis.

Changes in interest rates typically have a sizable effect on the fair values of our debt and equity securities. The interest rate of the ten-year U.S. Treasury bond increased slightly to 3.5% during the quarter ended March 31, 2011 from 3.3% at December 31, 2010. Net unrealized losses on fixed maturity securities totaled \$3.1 million at March 31, 2011 compared to losses of \$3.8 million at December 31, 2010.

The fixed maturity portfolio is exposed to call risk as a significant portion of the current bond holdings are callable. A decreasing interest rate environment can result in increased call activity, as experienced over the past several years, and an increasing rate environment will likely result in securities being paid at their stated maturity.

There are no fixed maturities or other investments classified as trading instruments. Approximately 90.4% of fixed maturities were held in available-for-sale and 9.6% in held-to-maturity based upon fair value at March 31, 2011. At March 31, 2011 and December 31, 2010, we had no investments in derivative instruments, nor did we have any

subprime or collateralized debt obligation risk.

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**CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011**

Market Risk Related to Equity Prices

Changes in the level or volatility of equity prices affect the value of equity securities we hold as investments. Our equity investments portfolio represented 3.1% of our total investments at March 31, 2011. We believe that significant decreases in the equity markets would not have a material adverse impact on our total investment portfolio.

Item 4. CONTROLS AND PROCEDURES

We have established disclosure controls and procedures to ensure, among other things, that material information relating to our Company, including its consolidated subsidiaries, is made known to our officers who certify our financial reports and to the other members of our senior management and the Board of Directors.

Our Chief Executive Officer and Chief Financial Officer are responsible for establishing and maintaining our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)). Based upon an evaluation at the end of the period, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report.

During the quarter ended March 31, 2011, there were no changes in the Company's internal controls over financial reporting that materially affect or are reasonably likely to affect the Company's internal controls over financial reporting (as defined in rules 13a-15(f) and 15d-15(f) under the Exchange Act).

PART II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

We are a defendant in a lawsuit filed on August 6, 1999 in the Texas District Court, Austin, Texas, now styled *Delia Bolanos Andrade, et al., Plaintiffs, v. Citizens Insurance Company of America, et al., Defendants* 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.

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**CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011**

Item 1A. RISK FACTORS

There are no updates to our risk factors as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2010.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. (RESERVED)

Item 5. OTHER INFORMATION

On May 5, 2011, the Company issued a news release (the Release) reporting, among other things, results for its first quarter 2011 earnings. A copy of the Release is furnished as Exhibit 99.1 to this Quarterly Report on Form 10-Q. Citizens also announced that it would hold a conference call to discuss its financial results at 10:00 a.m. Central Standard Time on Friday, May 6, 2011.

Item 6. EXHIBITS

Exhibit Number The following exhibits are filed herewith:

- 3.1 Restated and Amended Articles of Incorporation (a)
- 3.2 Bylaws (b)
- 4.1 Amendment to State Series A-1 and A-2 Senior Convertible Preferred Stock (c)
- 10.1 Self-Administered Automatic Reinsurance Agreement Citizens Insurance Company of America and Riunione Adriatica di Sicurta, S.p.A. (d)
- 10.2 Bulk Accidental Death Benefit Reinsurance Agreement between Connecticut General Life Insurance Company and Citizens Insurance Company of America, as amended (e)
- 10.3 Coinsurance Reinsurance Agreement, Assumption Reinsurance Agreement, Administrative Services Agreement dated March 9, 2004, between Citizens Insurance Company of America and Texas International Life Insurance Company, Reinsurance Trust Agreement dated March 9, 2004, by and among Citizens Insurance Company of America, Texas International Life Insurance Company and Wells Fargo Bank, N.A. (f)
- 10.4 Coinsurance Reinsurance Agreement, Assumption Reinsurance Agreement, Administrative Services Agreement dated March 9, 2004, between Combined Underwriters Life Insurance Company and Texas International Life Insurance Company, Reinsurance Trust Agreement dated March 9, 2004, by and among Combined Underwriters Life Insurance Company, Texas International Life Insurance Company and Wells Fargo Bank, N.A. (g)
- 10.5(a) Securities Purchase Agreement dated July 12, 2004 among Citizens, Inc., Mainfield Enterprises, Inc., Steelhead Investments Ltd., Portside Growth and Opportunity Fund, and Smithfield Fiduciary LLC (h)
- 10.5(b) Registration Rights Agreement dated July 12, 2004 among Citizens, Inc., Mainfield Enterprises, Inc., Steelhead Investments Ltd., Portside Growth and Opportunity Fund, and Smithfield Fiduciary

LLC (h)

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**CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011**

| | |
|----------------|--|
| Exhibit Number | The following exhibits are filed herewith: |
| 10.5(c) | Unit Warrant dated July 12, 2004, to Mainfield Enterprises, Inc. (h) |
| 10.5(d) | Unit Warrant dated July 12, 2004, to Steelhead Investments Ltd. (h) |
| 10.5(e) | Unit Warrant dated July 12, 2004, to Portside Growth and Opportunity Fund (h) |
| 10.5(f) | Unit Warrant dated July 12, 2004, to Smithfield Fiduciary LLC (h) |
| 10.5(g) | Warrant to Purchase Class A Common Stock to Mainfield Enterprises, Inc. (h) |
| 10.5(h) | Warrant to Purchase Class A Common Stock to Steelhead Investments Ltd. (h) |
| 10.5(i) | Warrant to Purchase Class A Common Stock to Portside Growth and Opportunity Fund (h) |
| 10.5(j) | Warrant to Purchase Class A Common Stock to Smithfield Fiduciary LLC (h) |
| 10.5(k) | Subordination Agreement among Regions Bank, the Purchasers and Citizens, Inc. dated July 12, 2004 (h) |
| 10.5(l) | Non-Exclusive Finder's Agreement dated September 29, 2003, between Citizens, Inc. and the Shemano Group, Inc. (h) |
| 10.6 | Self-Administered Automatic Reinsurance Agreement between Citizens Insurance Company of America and Converium Reinsurance (Germany) Ltd. (i) |
| 10.7 | Self-Administered Automatic Reinsurance Agreement between Citizens Insurance Company of America and Scottish Re Worldwide (England) (j) |
| 10.8 | Self-Administered Automatic Reinsurance Agreement CICA Life Insurance Company of America and Scor Global Life U.S. Re Insurance Company (k) |
| 10.9 | Self-Administered Automatic Reinsurance Agreement CICA Life Insurance Company of America and Mapfre Re Compania de Reaseguros, S.A. (l) |
| 11 | Statement re: Computation of per share earnings (see financial statements) |
| 21 | Subsidiaries of the Registrant* |
| 31.1 | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act* |
| 31.2 | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act* |
| 32.1 | Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act* |

- 32.2 Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act*
- 99.1 News Release reporting first quarter results issued on May 5, 2011 (furnished herewith).

* **Filed herewith.**

- (a) Filed on March 15, 2004 with the Registrant's Annual Report on Form 10-K for the Year Ended December 31, 2003 as Exhibit 3.1, and incorporated herein by reference.
- (b) Filed on March 31, 1999 with the Registrant's Annual Report on Form 10-K for the Year Ended December 31, 1998, as Exhibit 3.2, and incorporated herein by reference.
- (c) Filed on July 15, 2004, with the Registrant's Current Report on Form 8-K as Exhibit 4.1, and incorporated herein by reference.

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**CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
March 31, 2011**

- (d) Filed as Exhibit 10.8 with the Registration Statement on Form S-4, SEC File No. 333-16163, on November 14, 1996 and incorporated herein by reference.
- (e) Filed on April 9, 1997 as Exhibit 10.9 with the Registrant's Annual Report on Form 10-K for the Year Ended December 31, 1996, Amendment No. 1, and incorporated herein by reference.
- (f) Filed on March 22, 2004 as Exhibit 10.8 of the Registrant's Current Report on Form 8-K, and incorporated herein by reference.
- (g) Filed on March 22, 2004 as Exhibit 10.9 of the Registrant's Current Report on Form 8-K, and incorporated herein by reference.
- (h) Filed on July 15, 2004 as part of Exhibit 10.12 with the Registrant's Current Report on Form 8-K, and incorporated herein by reference.
- (i) Filed on March 31, 2005, with the Registrant's Annual Report on Form 10-K for the Year Ended December 31, 2004, as Exhibit 10.10(m), and incorporated herein by reference.
- (j) Filed on March 31, 2005, with the Registrant's Annual Report on Form 10-K for the Year Ended December 31, 2004, as Exhibit 10.10(n), and incorporated herein by reference.
- (k) Filed on November 6, 2009, with the Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2009, as Exhibit 10.8(k), and incorporated herein by reference.
- (l) Filed on November 6, 2009, with the Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2009, as Exhibit 10.9(l), and incorporated herein by reference.

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SIGNATURES

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

CITIZENS, INC.

By: /s/ Harold E. Riley
Harold E. Riley
Chairman and Chief Executive Officer

By: /s/ Kay E. Osbourn
Kay E. Osbourn
Executive Vice President, Chief
Financial Officer and Treasurer

Date: May 5, 2011