CITIZENS INC
Form 10-Q
November 07, 2008

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

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended September 30, 2008

or

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

Commission File Number: 000-16509

CITIZENS, INC.

(Exact name of registrant as specified in its charter)

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

(512) 837-7100
(Registrant s telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report.)

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

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

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

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

As of November 7, 2008 the Registrant had 43,824,117 Class A common stock outstanding and 1,001,714 shares of Class B common stock outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

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

Assets	September 30, 2008 (Unaudited)	December 31, 2007
Investments:		
Fixed maturities available-for-sale, at fair value (cost: $508,337 and $502,635 in 2008 and 2007, respectively)	$ 489,114	500,426
Equity securities available-for-sale, at fair value (cost: $60,680 and $36,696 in 2008 and 2007, respectively)	47,154	35,669
Mortgage loans on real estate	379	291
Policy loans	27,434	25,490
Real estate held for investment (less $277 and $249 accumulated depreciation in 2008 and 2007, respectively)	5,186	5,152
Other long-term investments	681	618
Short-term investments	7,965	17,650
Total investments	577,913	585,296
Cash and cash equivalents	45,670	21,123
Accrued investment income	6,228	7,115
Reinsurance recoverable	13,036	13,492
Deferred policy acquisition costs	106,002	100,655
Cost of customer relationships acquired	29,502	31,636
Goodwill	11,386	11,386
Other intangible assets	1,045	1,066
Federal income tax receivable	3,272	715
Deferred Federal income tax asset	2,958	
Property and equipment, net	6,574	6,795
Due premiums, net (less $1,774 and $1,780 allowance for doubtful accounts in 2008 and 2007, respectively)	7,190	7,656
Prepaid expenses	1,356	
Other assets	764	974
Total assets	$ 812,896	787,909

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)

Liabilities and Stockholders Equity	September 30, 2008 (Unaudited)	December 31, 2007
Liabilities:		
Future policy benefit reserves:		
Life insurance	$ 529,565	505,517
Annuities	24,394	22,792
Accident and health	7,485	8,293
Premiums paid in advance	18,931	16,140
Policy claims payable	9,171	6,908
Dividend accumulations	4,773	4,825
Other policyholders funds	7,266	7,049
Total policy liabilities	601,585	571,524
Commissions payable	1,901	2,385
Deferred Federal income tax		4,810
Payable for securities in process of settlement	18,058	7,000
Warrants outstanding	2,677	1,003
Other liabilities	11,389	10,810
Total liabilities	635,610	597,532
Commitments and contingencies (Note 7)		
Cumulative convertible preferred stock Series A (Series A-1 - $500 stated value per share, 18,750 and 25,000 shares authorized, issued and outstanding in 2008 and 2007, respectively; Series A-2 - $935 stated value per share, 5,000 shares authorized, 4,014 issued and outstanding in 2008 and 2007)	12,382	14,220
Stockholders Equity:		
Common stock:		
Class A, no par value, 100,000,000 shares authorized, 46,959,855 shares issued in 2008 and 46,205,830 shares issued in 2007, including shares in treasury of 3,135,738 in 2008 and 2007	228,830	225,812
Class B, no par value, 2,000,000 shares authorized, 1,001,714 shares issued and outstanding in 2008 and 2007	3,184	3,184
Retained deficit	(34,812)	(39,725)
Accumulated other comprehensive loss:		
Unrealized losses on securities, net of tax	(21,287)	(2,103)
	175,915	187,168

Treasury stock, at cost		(11,011)	(11,011)
Total stockholders equity		164,904	176,157
Total liabilities and stockholders equity	$	812,896	787,909

See accompanying notes to consolidated financial statements.

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

	2008	2007
Revenues:		
Premiums:		
Life insurance	$ 32,837	32,713
Accident and health insurance	384	359
Property insurance	820	1,188
Net investment income	7,543	7,354
Realized gains (losses), net	(226)	42
Increase in fair value of warrants	(1,483)	(300)
Other income	288	382
Total revenues	40,163	41,738
Benefits and expenses:		
Insurance benefits paid or provided:		
Claims and surrenders	13,855	12,696
Increase in future policy benefit reserves	10,214	8,656
Policyholders dividends	1,636	1,682
Total insurance benefits paid or provided	25,705	23,034
Commissions	8,819	8,906
Other underwriting, acquisition and insurance expenses	7,312	6,728
Capitalization of deferred policy acquisition costs	(5,712)	(6,576)
Amortization of deferred policy acquisition costs	3,861	3,010
Amortization of cost of customer relationships acquired and other intangibles	676	810
Total benefits and expenses	40,661	35,912
Income (loss) before Federal income tax	(498)	5,826
Federal income tax expense	316	1,169
Net income (loss)	$ (814)	4,657
Net income (loss) available to common stockholders	$ (1,604)	4,154
Per Share Amounts:		
Basic and diluted earnings (loss) per share of Class A common stock	$ (0.04)	0.10
Basic and diluted earnings (loss) per share of Class B common stock	$ (0.02)	0.05

See accompanying notes to consolidated financial statements.

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

		2008	2007
Revenues:			
Premiums:			
Life insurance	$	97,178	94,091
Accident and health insurance		1,178	1,162
Property insurance		3,559	3,550
Net investment income		22,487	21,485
Realized losses, net		(210)	(90)
Increase in fair value of warrants		(1,674)	(496)
Other income		852	1,167
Total revenues		123,370	120,869
Benefits and expenses:			
Insurance benefits paid or provided:			
Claims and surrenders		41,663	37,900
Increase in future policy benefit reserves		24,944	23,980
Policyholders dividends		4,590	4,334
Total insurance benefits paid or provided		71,197	66,214
Commissions		25,906	26,292
Other underwriting, acquisition and insurance expenses		21,243	20,952
Capitalization of deferred policy acquisition costs		(16,876)	(19,482)
Amortization of deferred policy acquisition costs		11,529	9,490
Amortization of cost of customer relationships acquired and other intangibles		2,155	2,477
Total benefits and expenses		115,154	105,943
Income before Federal income tax		8,216	14,926
Federal income tax expense		3,303	4,303
Net income	$	4,913	10,623
Net income available to common stockholders	$	3,112	9,106
Per Share Amounts:			
Basic and diluted earnings per share of Class A common stock	$	0.07	0.22
Basic and diluted earnings per share of Class B common stock	$	0.04	0.11

See accompanying notes to consolidated financial statements.

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

	2008	2007
Cash flows from operating activities:		
Net income	$ 4,913	10,623
Adjustments to reconcile net income to net cash provided by operating activities:		
Realized losses on sale of investments and other assets	210	90
Net deferred policy acquisition costs	(5,347)	(9,992)
Amortization of cost of customer relationships acquired and other intangibles	2,155	2,477
Increase in fair value of warrants	1,674	496
Depreciation	827	752
Amortization of premiums and discounts on fixed maturities and short-term investments	216	995
Deferred Federal income tax expense (benefit)	2,562	(530)
Change in:		
Accrued investment income	887	510
Reinsurance recoverable	456	2,183
Due premiums and other receivables	591	169
Future policy benefit reserves	21,372	22,099
Other policy liabilities	7,911	(241)
Federal income tax receivable	(2,557)	(2,977)
Commissions payable and other liabilities	95	(3,823)
Other, net	(1,270)	(761)
Net cash provided by operating activities	34,695	22,070
Cash flows from investing activities:		
Sale of fixed maturities, available-for-sale	237	3,344
Maturity and calls of fixed maturities, available-for-sale	130,800	49,256
Purchase of fixed maturities, available-for-sale	(126,514)	(63,648)
Sale of equity securities, available-for-sale		20
Purchase of equity securities, available-for-sale	(23,984)	(17,097)
Principal payments on mortgage loans	27	156
Mortgage loans funded	(115)	
Sale of other long-term investments and property and equipment	178	342
Purchase of other long-term investments and property and equipment	(868)	(4,009)
Increase in policy loans	(1,944)	(1,930)
Maturity of short-term investments	18,000	
Purchase of short-term investments	(7,923)	

Net cash used in investing activities	$	(12,106)	(33,566)

See accompanying notes to consolidated financial statements.

(Continued)

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Consolidated Statements of Cash Flows, Continued
Nine Months Ended September 30
(In thousands)
(Unaudited)

	2008	2007
Cash flows from financing activities:		
Annuity deposits	$ 1,862	1,640
Annuity withdrawals	(1,084)	(1,492)
Series A-1 Preferred Stock capital contribution	1,125	
Warrant exercise	55	
Net cash provided by financing activities	1,958	148
Net increase (decrease) in cash and cash equivalents	24,547	(11,348)
Cash and cash equivalents at beginning of period	21,123	24,521
Cash and cash equivalents at end of period	$ 45,670	13,173
Supplemental disclosures of operating activities:		
Cash paid during the period for income taxes	$ 3,298	7,810

Supplemental Disclosures of Non-Cash Financing Activities:
Dividends on the Company s Series A-1 Convertible Preferred Stock, issued in 2004, and Series A-2 Convertible Preferred Stock, issued in 2005, were paid by the Company through the issuance of Class A common stock to the preferred shareholders in the amount of $514,000 for the first nine months of 2008 and 2007. Accretion of deferred issuance costs and discounts on the Convertible Preferred Stock recorded as a deduction to Class A common stock during the first nine months of 2008 and 2007 was $1.3 million and $1.0 million, respectively.
See accompanying notes to consolidated financial statements.

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CITIZENS, INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
September 30, 2008
(Unaudited)

(1) Financial Statements

The interim consolidated financial statements include the accounts and operations of Citizens, Inc. (Citizens), incorporated in the state of Colorado on November 8, 1977, and its wholly-owned subsidiaries, CICA Life Insurance Company of America (CICA), Computing Technology, Inc. (CTI), Funeral Homes of America, Inc. (FHA), Insurance Investors, Inc. (III), Citizens National Life Insurance Company (CNLIC), Security Plan Life Insurance Company (SPLIC), and Security Plan Fire Insurance Company (SPFIC). Citizens and its consolidated subsidiaries are collectively referred to as the Company, we, or our.

The consolidated statement of financial position as of September 30, 2008, the consolidated statements of operations for the three and nine-month periods ended September 30, 2008 and 2007, and the consolidated statements of cash flows for the nine-month periods then ended have been prepared by the Company without audit. In the opinion of management, all adjustments to present fairly the financial position, results of operations and changes in cash flows at September 30, 2008, and for comparative periods presented have been made.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with United States of America (U.S.) Generally Accepted Accounting Principles (U.S. GAAP) have been omitted. It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007. The results of operations for the nine months ended September 30, 2008, are not necessarily indicative of the operating results for the full year.

At December 31, 2007, the Security Plan in force policies were converted to the Company s mainframe policy administration system and Security Plan s original computer system was discontinued, except for providing access to certain historical information. The initial conversion was successful and all in force amounts were reconciled between systems. The Company recognized, due to the uniqueness of the home service business, that some actuarial estimates will be necessary until ongoing system modifications and enhancements are completed some time in 2008. These actuarial estimates were not necessary in 2007. They were included in Security Plans valuation system in the prior year.

During the first quarter of 2008, the Company discovered an overstatement of life reserves, due to the use of an incorrect reserve factor going back several years, in the amount of $796,000. The error was corrected during the first quarter, resulting in an increase to net income of $517,000 during the first quarter.

Reclassifications

The Company has previously accounted for the conversion of a policy from premium paying to extended term insurance (ETI) as the surrender of the premium paying policy for its cash value, with the cash value being applied as a single premium to purchase the ETI policy. Thus, premiums and surrenders were overstated by the amount of this single premium. Beginning in the first quarter of 2008, the Company no longer accounts for the conversion of a premium paying policy to ETI as a surrender of one policy and simultaneous purchase of a single premium policy. To effect this change, prior year life premiums have been reduced by $1,069,000 and $2,967,000 for the three months and nine months ended September 30, 2007, respectively, with a corresponding reduction in claims and surrenders. For the full year 2007, the amount of this reclassification was $4,157,000.

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During the third quarter of 2008, the Company completed the conversion of SPLIC s supplemental contracts without life contingencies (SCWOLC) to our mainframe policy administration system. In conjunction with this conversion, the SCWOLC account balance at December 31, 2007 in the amount of $2,692,000 was reclassified out of life insurance future policy benefit reserves into other policyholders funds on the consolidated statement of financial position.

(2) Accounting Pronouncements

In December 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 141 (Revised 2007), *Business Combinations* (FAS 141R) and SFAS No. 160, *Accounting and Reporting of Non-controlling Interests in Consolidated Financial Statements*, an amendment to ARB No. 51 (SFAS 160). These two standards must be adopted in conjunction with each other on a prospective basis. FAS 141R will significantly change the accounting for business combinations in a number of areas including the treatment of contingent consideration, contingencies, acquisition costs, research and development assets and restructuring costs. In addition, under FAS 141R, changes in deferred tax asset valuation allowances and acquired income tax uncertainties in a business combination after the measurement period will impact income taxes. FAS 141R is effective for fiscal years beginning after December 15, 2008. The Company will determine the impact of adopting FAS 141R on its consolidated financial statements, should applicable transactions occur in the future.

In April 2008, the FASB issued Staff Position (FSP) No. 142-3, *Determining the Useful Life of Intangible Assets* (FSP 142-3). FSP 142-3 amends the factors to be considered in determining the useful life of intangible assets. Its intent is to improve the consistency between the useful life of an intangible asset and the period of expected cash flows used to measure such asset s fair value. FSP 142-3 is effective for fiscal years beginning after December 15, 2008. The Company is currently assessing the potential impact, if any, of FSP 142-3 on its financial statements.

As of January 1, 2008, the Company adopted SFAS No. 157 (FAS 157), *Fair Value Measurements*. This Statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. The adoption of FAS 157 did not have a material impact on our consolidated financial statements. Additionally, on January 1, 2008, the Company elected the partial adoption of FAS 157 under the provisions of FSP No. 157-2, which amends FAS 157 to allow an entity to delay the application of this statement until January 1, 2009 for certain non-financial assets and liabilities. Under the provisions of the FSP, we will delay the application of FAS 157 for fair value measurements used in the impairment testing of goodwill and indefinite-lived intangible assets and eligible non-financial assets and liabilities included within a business combination. In January, 2008, FASB also issued proposed FSP FAS No. 157-c that would amend FAS 157 to clarify the principles on fair value measurement of liabilities. Management is monitoring the status of this proposed FSP for any impact on our consolidated financial statements. On October 10, 2008, the FASB issued FSP FAS No. 157-3 to clarify the application of fair value measurements of a financial asset when the market for that asset is not active. This clarifying guidance became effective upon issuance, including prior periods for which financial statements had not been issued, such as the period ended September 30, 2008 for the Company. The adoption of FSP FAS 157-3 had no impact on the Company s results of operations or financial position. See Note 6 for additional disclosures about fair value measurement.

As of January 1, 2008, the Company adopted SFAS No. 159 (FAS 159), *The Fair Value Option for Financial Assets and Financial Liabilities*. This Statement provides an option, on specified election dates, to report selected financial assets and liabilities, including insurance contracts, at fair value. Subsequent changes in fair value for designated items are reported in income in the current period. The adoption of FAS 159 did not impact our consolidated financial statements, as no items were elected for measurement at fair value upon initial adoption. We will continue to evaluate eligible financial assets and liabilities on their election dates. Any future elections will be disclosed in accordance with the provisions outlined in the Statement.

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(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 net income before federal income taxes for its three reportable segments.

The allocation of expenses within the Citizens, Inc. management services agreement was changed in the first quarter of 2008 to reflect the conversion of Security Plan s policies to our policy administration system at year end 2007. Approximately $1.0 million in expenses per quarter were reallocated from the Life Insurance segment to the Home Service segment, which is reflected in the lower profits for the Home Service segment compared to comparable periods in 2007.

The measurement of segment profit and loss and segment assets do not include material transactions between segments. The Company has no reportable differences between segments and consolidated operations.

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The following summary presents the Company s profit (loss) measurement from continuing operations for each reportable segment, along with certain components of that profit (loss) measurement, for the periods indicated.

	Three Months Ended September 30,	
	2008	2007
	(In thousands)	
Profit (Loss) Measurement		
Income (loss) before federal income tax:		
Life Insurance	$ 2,687	2,862
Home Service Insurance	(2,317)	3,507
Other Non-Insurance Enterprises	(868)	(543)
Total consolidated pretax income (loss)	$ (498)	5,826
Selected Components of Profit (Loss) Measurement		
Revenue:		
Life Insurance	$ 28,810	28,640
Home Service Insurance	12,476	13,212
Other Non-Insurance Enterprises	(1,123)	(114)
Total consolidated revenue	$ 40,163	41,738
Premiums:		
Life Insurance	$ 24,634	24,429
Home Service Insurance	9,407	9,831
Other Non-Insurance Enterprises		
Total consolidated premiums	$ 34,041	34,260
Net investment income:		
Life Insurance	$ 4,309	3,952
Home Service Insurance	3,072	3,384
Other Non-Insurance Enterprises	162	18
Total consolidated net investment income	$ 7,543	7,354
Amortization expense:		
Life Insurance	$ 3,709	2,716
Home Service Insurance	828	1,104
Other Non-Insurance Enterprises		

Total consolidated amortization expense	$	4,537	3,820
Net realized gains (losses) on sale of investments and other assets:			
Life Insurance	$	(223)	49
Home Service Insurance		(3)	(7)
Other Non-Insurance Enterprises			
Total consolidated net realized gains (losses)	$	(226)	42

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The following summary presents the Company s profit (loss) measurement from continuing operations for each reportable segment, along with certain components of that profit (loss) measurement, for the periods indicated.

	Nine Months Ended September 30,	
	2008	2007
	(In thousands)	
Profit (Loss) Measurement		
Income (loss) before federal income tax:		
Life Insurance	$ 8,919	7,368
Home Service Insurance	(110)	8,540
Other Non-Insurance Enterprises	(593)	(982)
Total consolidated pretax income	$ 8,216	14,926
Selected Components of Profit (Loss) Measurement		
Revenue:		
Life Insurance	$ 85,129	81,417
Home Service Insurance	38,589	39,182
Other Non-Insurance Enterprises	(348)	270
Total consolidated revenue	$ 123,370	120,869
Premiums:		
Life Insurance	$ 72,584	69,278
Home Service Insurance	29,331	29,525
Other Non-Insurance Enterprises		
Total consolidated premiums	$ 101,915	98,803
Net investment income:		
Life Insurance	$ 12,519	11,541
Home Service Insurance	9,255	9,736
Other Non-Insurance Enterprises	713	208
Total consolidated net investment income	$ 22,487	21,485
Amortization expense:		
Life Insurance	$ 10,768	9,192
Home Service Insurance	2,916	2,775
Other Non-Insurance Enterprises		

Total consolidated amortization expense	$	13,684	11,967
Net realized gains (losses) on sale of investments and other assets:			
Life Insurance	$	(220)	6
Home Service Insurance		(8)	(84)
Other Non-Insurance Enterprises		18	(12)
Total consolidated net realized losses	$	(210)	(90)

		September 30, 2008	December 31, 2007
		(In thousands)	
Assets:			
Life Insurance	$	476,311	449,719
Home Service Insurance		300,564	305,997
Other Non-Insurance Enterprises		36,021	32,193
Total consolidated assets	$	812,896	787,909

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(4) Total Comprehensive Income (Loss)

	Three Months Ended September 30,	
	2008	2007
	(In thousands)	
Net income (loss)	$ (814)	4,657
Other comprehensive income (loss), net of tax:		
Unrealized net gains (losses) on investments in fixed maturities available for sale and equity securities available for sale	(12,916)	4,919
Total comprehensive income (loss)	$ (13,730)	9,576

	Nine Months Ended September 30,	
	2008	2007
	(In thousands)	
Net income	$ 4,913	10,623
Other comprehensive income (loss), net of tax:		
Unrealized net gains (losses) on investments in fixed maturities available for sale and equity securities available for sale	(19,184)	1,639
Total comprehensive income (loss)	$ (14,271)	12,262

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(5) Earnings per Share

The following tables set forth the computation of basic and dilutive earnings per share for the periods indicated:

	Three Months Ended September 30, 2008	2007
	(In thousands, except per share amounts)	
Basic and diluted earnings (loss) per share:		
Numerator:		
Net income (loss)	$ (814)	4,657
Less: Preferred stock dividends	(171)	(169)
Accretion of deferred issuance costs and discounts on preferred stock	(619)	(334)
Net income (loss) available to common stockholders	$ (1,604)	4,154
Net income (loss) allocated to Class A common stock	$ (1,585)	4,103
Net income (loss) allocated to Class B common stock	(19)	51
Net income (loss) available to common stockholders	$ (1,604)	4,154
Denominator:		
Weighted average shares of Class A outstanding basic and diluted	43,198	40,338
Weighted average shares of Class B outstanding basic and diluted	1,002	1,002
Total weighted average shares outstanding basic and diluted	44,200	41,340
Basic and diluted earnings (loss) per share of Class A common stock	$ (0.04)	0.10
Basic and diluted earnings (loss) per share of Class B common stock	$ (0.02)	0.05

		Nine Months Ended September 30,	
		2008	2007
		(In thousands, except per share amounts)	
Basic and diluted earnings per share:			
Numerator:			
Net income	$	4,913	10,623
Less: Preferred stock dividends		(514)	(514)
Accretion of deferred issuance costs and discounts on preferred stock		(1,287)	(1,003)
Net income available to common stockholders	$	3,112	9,106
Net income allocated to Class A common stock	$	3,076	8,994
Net income allocated to Class B common stock		36	112
Net income available to common stockholders	$	3,112	9,106
Denominator:			
Weighted average shares of Class A outstanding basic and diluted		43,121	40,313
Weighted average shares of Class B outstanding basic and diluted		1,002	1,002
Total weighted average shares outstanding basic and diluted		44,123	41,315
Basic and diluted earnings per share of Class A common stock	$	0.07	0.22
Basic and diluted earnings per share of Class B common stock	$	0.04	0.11

The effects of Series A-1 and A-2 Convertible Preferred Stock and warrants are anti-dilutive; therefore, diluted income per share is reported the same as basic income per share. The Series A-1 and A-2 Convertible Preferred Stock is anti-dilutive because the amount of the dividends and accretion of deferred issuance costs and discounts for the nine months ended September 30, 2008 per Class A common stock share obtainable on conversion exceeds basic income per share available to common stockholders. The warrants are anti-dilutive because the exercise price is in excess of the average Class A common stock market price for the nine months ended September 30, 2008.

(6) Fair Value Measurements

As defined in FAS 157, 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 fixed maturity and equity securities that 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. FAS 157 requires all assets and liabilities carried at fair value 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.

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

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

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

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

	September 30, 2008 (In thousands)			
	Total	**Level 1**	**Level 2**	**Level 3**
Financial Assets:				
Fixed Maturities Available-for-Sale	$ 489,114	12,947	475,494	673
Equity Securities Available-for-Sale	47,154	47,154		
Total Financial Assets	$ 536,268	60,101	475,494	673

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

September 30, 2008 (In thousands)	
Beginning balance at December 31, 2007	$ 700
Total realized and unrealized gains (losses):	
Included in net income	
Included in other comprehensive income	(3)
Principal paydowns	(24)
Transfer in and (out) of Level 3	
Ending balance at September 30, 2008	$ 673

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, if any, are reported as transfers in and out of Level 3 at the beginning fair value for the reporting period in which the changes occur.

(7) Legal Proceedings

We are a defendant in a lawsuit originally filed on August 6, 1999 in the Texas District Court, Austin, Texas, now styled *Citizens Insurance Company of America, Citizens, Inc., Harold E. Riley and Mark A. Oliver, Petitioners v. Fernando Hakim Daccach*, *Respondent*, in which a class was originally certified by the trial court and affirmed by the Court of Appeals for the Third District of Texas. We appealed the grant of class status to the Texas Supreme Court, which on March 2, 2007, reversed the Court of Appeal s affirmation of the trial court s class certification order, decertified the class and remanded the case to the trial court for further proceedings consistent with the Texas Supreme Court s opinion. As a result, no class action is presently certified, and plaintiffs counsel is seeking to recertify the class. In order to recertify the class, the lead plaintiff must establish that he is qualified to represent the purported class and that the res judicata effect of a class action will not have a deleterious effect on the putative class members. The underlying lawsuit alleges that certain life insurance policies that we 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. We believe the lawsuit is without merit and intend to continue a vigorous defense in any remaining proceedings, including any class recertification. If the class is recertified, we could be exposed to costly and time-consuming litigation, and an adverse judgment could have a material adverse effect on our results of operations and financial condition. The case is now before the District Court judge for an analysis of the evidence presented to determine if it warrants recertification of a class.

SPFIC is a defendant in a suit styled *The State of Louisiana v. AAA Insurance*, or *Road Home Litigation*, which was filed in the Civil District Court for the Parish of Orleans on August 23, 2007 by the state of Louisiana as subrogee/assignee of the insureds of more than 200 different insurance companies. The suit was filed to recover money that the state of Louisiana paid to certain insureds under the Louisiana Road Home Program for damages resulting from Hurricanes Katrina and Rita. The suit was removed to the United States District Court for the Eastern District of Louisiana on September 11, 2007 and appeals of the removal have been denied. Responsive pleadings have not yet been filed on behalf of any of the defendant insurers in this case, nor has any discovery been conducted to date.

SPFIC was also named as a defendant in a lawsuit filed in the Civil District Court for the Parish of Orleans on behalf of Karen Cheneau in August 2006. The *Cheneau* suit stems from damages Ms. Cheneau sustained during Hurricane Katrina. In November 2007, plaintiff filed a Motion for Leave to File First Amended Petition to Assert Class Allegations against SPFIC. The purported class consists of Louisiana citizens who purchased homeowner s insurance coverage and/or contents insurance coverage from SPFIC, whose homes and/or property covered by said policies were damaged as a result of Hurricane Katrina and who timely submitted claims to SPFIC for their losses, and who either received no recovery or received less than the alleged proper value of their valued policies as a result of their claims. SPFIC has responded to the Amended Petition by filing Exceptions of No Cause of Action, No Right of Action, Vagueness, Prescription and Failure to Meet Class Action Requirements. In April 2008, the Plaintiff s local counsel in Louisiana filed an Ex Parte Motion to Withdraw from the case. Currently, the Plaintiffs are without local counsel to file pleadings and attend hearings on their behalf. The Exceptions have not yet been set for hearing. SPFIC intends to vigorously defend this lawsuit.

The *Road Home Litigation* and *Cheneau* are in the early stages of litigation, and no discovery has yet occurred. Therefore, it is not possible to evaluate how many claims in those cases relate to SPFIC, or the potential exposure to SPFIC. However, in the event of an adverse outcome, the potential exposure to SPFIC could be significant.

On November 8, 2005, SPLIC was named as a defendant in a suit styled *Lilac Todd vs. Security Plan Life Insurance Company*, on behalf of Lilac Todd, which alleges that SPLIC failed to pay Ms. Todd s claim for medical expenses arising out of the loss of one of her limbs. On December 20, 2007, a Supplemental and Amended Petition for Damages was filed pursuant to which the plaintiff has asserted class action allegations. The purported class is defined as all Louisiana insureds of SPLIC whose policies contained an incontestability provision identical or similar to Ms. Todd s policy, and whose claims were denied within 10 years of the petition filing on the basis of illnesses, injuries or diseases diagnosed or which occurred at any time preceding the incontestability.

This matter is in the early stages of litigation relative to the class allegations. Plaintiffs have not established how many, if any, individuals are within the class definition proposed by plaintiff. SPLIC intends to aggressively defend this action. However, in the event of an adverse outcome, the potential exposure to SPLIC could be significant.

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In addition to the legal proceedings 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. We have not established any material reserve account on our consolidated financial statements for the adverse financial impact of any of our litigation matters.

(8) Convertible Preferred Stock

In July 2004, we completed a private placement of $12.5 million of Series A-1 Convertible Preferred Stock (Series A-1 Preferred) to four unaffiliated institutional investors. The Company also issued to the investors warrants to purchase 544,000 shares of Class A common stock, at an exercise price of $6.95 per share, and unit warrants to purchase Series A-2 Convertible Preferred Stock (Series A-2 Preferred). The conversion, exercise and redemption prices set forth in this Note 8, along with the numbers of shares and warrants (except for the 25,000 Series A-1 Preferred shares referenced below), have been adjusted for the common stock dividends paid December 31, 2004 and December 31, 2005.

The Series A-1 and A-2 Preferred Stock is mandatorily redeemable in 2009. Both may also become redeemable at the option of the holder if certain conditions exist. The shares will be redeemed in shares of Class A common stock unless certain conditions are met to allow redemption in cash. If redeemed in stock, the redemption price is based on a defined formula.

In the third quarter of 2008, one of the Series A-1 Preferred Stock investors converted out of their position into Class A common stock at a conversion price of $6.33. This resulted in the issuance of 493,680 shares of Class A common stock plus their accrued dividend worth 3,846 shares. The Company accelerated the accretion on this block of Series A-1 Preferred Stock during the quarter resulting in additional accretion of $284,000. Also during the third quarter of 2008, another holder of the Series A-1 Preferred Stock increased their stated value from $500 a share to $680 a share by sending the Company a capital contribution in the amount of $1.1 million. The holder then immediately converted the capital contribution, at a conversion price of $6.33, into Class A common stock, resulting in the issuance of 177,725 shares of Class A common stock.

One of the finders of the Series A Preferred Stock also exercised warrants to purchase 8,000 shares of Class A common stock in the third quarter of 2008 at a strike price of $6.95.

At September 30, 2008 and December 31, 2007, there was $267,000 and $583,000 in unaccreted deferred issuance costs and $478,000 and $1,449,000 in unaccreted net discount costs, respectively. The redemption value of the series A-1 and A-2 convertible stock was $13,126,000 at September 30, 2008.

(9) Subsequent Events

On October 27, 2008, the Company completed its acquisition of Ozark National Life Insurance Company of Little Rock, Arkansas for $8.0 million in cash. On a statutory basis of accounting, Ozark National had regulatory assets of $18.5 million, capital and surplus of $1.8 million, and annual premiums and deposits of $4.0 million, as of the year

ended December 31, 2007.

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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 us with the Securities and Exchange Commission, in press releases, and in oral and written statements made by or with our approval, 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, expects, intends, targeted, may, will and similar expressions are intended to identify forward-looking statements but are not the exclusive means of identifying such statements.

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

- ***Changes in foreign and U.S. general economic conditions, including the performance of financial markets and interest rates;***
- ***Changes in consumer behavior, which may affect our ability to sell our 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 our products;***
- ***Changes in assumptions related to deferred acquisition costs and the value of business acquired;***
- ***Regulatory, accounting or tax changes that may affect the cost of, or the demand for, our products or services; and***
- ***Our concentration of business from persons residing in Latin America and the Pacific Rim; and, our success at managing the risks involved in the foregoing.***

Such forward-looking statements speak only as of the date on which such statements are made, and we undertake 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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Overview

We are an insurance holding company serving the life insurance needs of individuals in the United States and in more than 35 countries around the world. We pursue a strategy of offering ordinary whole life insurance with a focus on cash accumulation and final expense insurance products in niche markets where we believe we are able to achieve competitive advantages. Our core operations include issuing and servicing:

- U.S. Dollar-denominated ordinary whole life insurance policies predominantly to high net worth, high income foreign residents, principally in Latin America and the Pacific Rim, through approximately 2,350 independent marketing consultants;

- ordinary whole life insurance policies to middle income households in the Midwest and the southern United States through approximately 400 independent marketing consultants; and

- final expense and limited liability property policies to middle and lower income households in Louisiana through approximately 320 employee agents in our home service distribution channel.

We primarily operate through two segments as follows:

Life Insurance. For more than 30 years, CICA and its predecessors have participated in the foreign marketplace through the issuance of U.S. Dollar-denominated ordinary whole life insurance to foreign nationals. Traditionally, this market has focused on the top 3-5% of the population of a country in terms of income and net worth. In recent years, however, there has been a shift to encompass a broader spectrum of the population, as upper middle classes develop in Latin America and the Pacific Rim. We make our insurance products available using third-party marketing organizations and independent marketing consultants. The number of our producing independent consultants has expanded over the years in this segment to approximately 2,350, and we presently receive applications from more than 35 countries outside of the U.S. Historically, the majority of our international business has come from Latin America. However, in 2004 the Pacific Rim began to represent a meaningful and growing source of new business.

In the first nine months of 2008, our Life Insurance segment generated revenue of $85.1 million, which accounted for 69.0% of our total revenue, compared to revenue of $81.4 million, or 67.4% of total revenue for the same period in 2007. In the second quarter of 2008, CICA introduced a new set of international life insurance products. We anticipate these new products will be well received in the international market. Our strategy in operating our Life Insurance segment is to increase new business written through our existing marketers as well as recruit new marketers and expand the number of countries from which we receive policy applications.

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

Home Service Insurance. Through a subsidiary, SPLIC, we provide final expense ordinary life insurance to middle and lower income individuals, primarily in Louisiana. Our policies in this segment are sold and serviced through the home service marketing distribution system utilizing employee-agents who work on a route system to collect premiums and service policyholders.

At December 31, 2007, the Security Plan in force policies were transitioned to the Company s integrated policy administration system and Security Plan s original computer system was eliminated for production purposes and continues to be available only for historical information inquiry. The conversion was successful and all in force amounts were reconciled between systems. The Company recognized, due to the uniqueness of home service business, that some actuarial estimates would be necessary on an interim basis until the home service administrative modifications and enhancements are completed later in 2008 or early 2009.

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During the first nine months of 2008, revenue from this segment was $38.6 million, which accounted for 31.3% of our total revenue, compared to revenue from this segment of $39.2 million, or 32.4% of total revenue, during the same period in 2007. Our business strategy in this segment is to continue to serve existing customers in Louisiana as well as expand the business through the acquisition of similar operations. Premiums were adversely affected by Hurricane Gustav, which hit Louisiana in the third quarter of 2008, as SPFIC had to pay additional catastrophe reinsurance premiums of $478,000 for second event reinstatement and third event coverage on potential future hurricanes in 2008.

Marketplace Conditions and Trends

Described below are some of the significant recent events and trends affecting the life insurance industry and the possible effects they may have on our future operations.

As an increasing percentage of the world population reaches retirement age, we believe we will benefit from increased demand for living products rather than death products, as aging baby boomers will require cash accumulation to provide expenses to meet their lifetime needs. Our ordinary life products are designed to accumulate cash values to provide for living expenses in a policy owner s later years, while continuously providing a death benefit.

We are exposed to a variety of risks, including the current market conditions as well as the credit crisis and corresponding potential changes in the fair value of our investments. In the normal course of business, we employ established policies and procedures to manage our exposure to fluctuations in the current market and changes in the fair value of our investments. We have not experienced any significant impairment in the value of our securities due to the current credit crisis in world financial markets. An immaterial impairment was recorded in the third quarter of 2008 as noted below. We have no subprime or collateralized debt investments.

The volatility in the equity markets over the past few years has posed a number of problems for some companies in the life insurance industry. Our equity holdings have been limited to 8.2% of total invested assets as of September 30, 2008 and 6.1% at December 31, 2007.

Corporate bond defaults and credit downgrades, which have resulted in other-than-temporary impairments in the value of some securities, have had a material impact on life insurers in the past few years. The Company recorded a loss of $223,000 during the quarter ended September 30, 2008, resulting from the other-than-temporary impairment of one Lehman Brothers bond holding. No bond other-than-temporary impairments were taken during 2007. The majority of our investment portfolio is held in debt instruments in U.S. Government-sponsored enterprises. Most of the municipal bonds we own are privately insured. We intend to manage our investment portfolio in the future using these types of debt instruments. At September 30, 2008, 71.5% of our fixed maturity securities were invested in U.S. Government-sponsored enterprises, including Fannie Mae and Freddie Mac. The recent stock market turmoil related to these companies has not affected our bond holdings in these entities. The Company continues to monitor these investments, and has not seen any material decrease in the prices of these bonds.

Because of the trends described above coupled with increasing costs of regulatory compliance such as the Sarbanes-Oxley Act of 2002, we believe there is a trend towards consolidation of domestic life insurance companies. We believe this should be a benefit to our acquisition strategy because there should be more complementary acquisition candidates available for us to consider.

Many of the events and trends affecting the life insurance industry have had an impact on the life reinsurance industry. These events led to a decline in the availability of reinsurance. While we currently cede a limited amount of our primary insurance business to reinsurers, we may find it difficult to obtain reinsurance in the future, forcing us to seek reinsurers who are more expensive to us. If we cannot obtain affordable reinsurance coverage, either our net exposures will increase or we will have to reduce our underwriting commitments.

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Quarter Ended September 30, 2008 Compared to Quarter Ended September 30, 2007

All comparisons below state the 2008 third fiscal quarter first and the 2007 third fiscal quarter second.

Consolidated Results of Operations

We incurred a net loss of $814,000 compared to net income of $4.7 million for the same period of 2007. The primary causes of this variance was due to a decrease in income in the Home Service segment. This was caused by property losses incurred by SPFIC from Hurricanes Gustav and Ike, higher commissions, and higher death claims. This resulted in a loss of $2.3 million for the quarter in the Home Service segment. Additionally, in the consolidated results of operations there was a loss from an increase in fair value of warrants associated with the Company s preferred stock and higher expenses.

Total consolidated revenues were $40.2 million, a 3.8% decrease compared to $41.7 million. Total revenues from our Life Insurance segment amounted to $28.8 million, compared to $28.6 million. Total revenues from Home Service were $12.5 million during the third quarter of 2008 and $13.2 million during the same period in 2007.

During the quarter, SPFIC was impacted by two hurricanes, Gustav and Ike. The Company has catastrophic reinsurance covering both events. Claims from Hurricane Gustav will exceed $3.2 million, but are reinsured above our retention of $500,000. Hurricane Ike is expected to be a less significant event. The financial statement impact of both hurricanes for the quarter was approximately $1.1 million. The incurred loss on Gustav included our $500,000 retention limit and reinsurance reinstatement premiums of $478,000. Reserves for Hurricane Ike were $135,000. Additionally, $104,000 in reserves was accrued related to ongoing litigation on disputed claims from Hurricane Katrina, which occurred on 2005. The Company believes it is properly reserved for these storms, and does not anticipate future losses.

Premium Income. Premium income decreased to $34.0 million from $34.3 million. The decrease was attributable to a slowdown in new business written internationally, as well as additional casualty reinsurance premiums. International business is down, due to a longer than anticipated acceptance period for our new products, and market disruptions in some of our larger areas.

Net Investment Income. Net investment income increased 2.6% to $7.5 million compared to $7.4 million, due primarily to the growth in our investment portfolio during 2008. Additionally, during 2007 and through the third quarter of 2008, we invested $60.7 million in equity mutual funds. We expect to use equity mutual fund investments of about 10% of total invested assets to diversify our holdings. We continue to invest primarily in bonds of U.S. Government-sponsored enterprises, such as Fannie Mae and Freddie Mac.

Increase in Fair Value of Warrants. We incurred a loss on the increase in fair value of warrants of $1.5 million in 2008 compared to a loss of $300,000 in 2007. The sizeable loss in 2008 was directly related to the increase in the price of our Class A common stock, as well as an increase in volatility. The warrant liability is calculated using the Black-Scholes option pricing model, which attempts to predict the value of the options when they expire in July 2011 and 2012. Current accounting standards require that the change in the value of the warrant liability is a component of revenues. When the liability goes up we incur a loss, and when the liability goes down we generate income. The warrant liability has no affect on the Company s cash flows, as the Company expects the warrants will be converted into our Class A common stock in July 2011, or sooner, at the election of the warrant holders, or expire.

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Claims and Surrenders. As noted in the table below, claims and surrenders increased to $13.9 million from $12.7 million, due primarily to an increase in property claims and an increase in endowment benefits.

	Three Months Ended September 30,	
	2008	2007
	(In thousands)	
Death claims	$ 5,156	5,215
Surrender benefits	3,591	3,680
Endowments	3,415	3,152
Property claims	1,178	(176)
Other policy benefits	419	732
Accident and health benefits	96	93
Total claims and surrenders	$ 13,855	12,696

Endowments were up $263,000, or 8.3%, as maturities within the block of business that features the endowment benefit continue to grow. This benefit is priced into the premium and does not have a negative impact on results of operations.

Property claims were up $1.4 million. Hurricanes Gustav and Ike swept through Louisiana during the third quarter of 2008, accounting for $635,000 of the increase. During the third quarter of 2007, we released reserves of $524,000 related to the 2005 hurricanes.

Change in Reserves. Reserves increased from $8.7 million in 2007 to $10.2 million in 2008. There were $1.0 million of reserve increases in the third quarter that related to the manual lapse adjustment in the second quarter. This adjustment was for policies which paid up in the third quarter or were adjustments to the original estimate.

Other Underwriting, Acquisition and Insurance Expenses. Expenses increased to $7.3 million from $6.7 million, primarily due to an increase in staff at the Austin office, as well as a $161,000 increase in international shipping costs.

Deferred Policy Acquisition Costs. Capitalized deferred policy acquisition costs (DAC) decreased 13.1% to $5.7 million from $6.6 million. This was also a direct consequence of reduced international new business production, as less commissions and expenses were capitalized. Amortization of these costs was $3.9 million and $3.0 million in 2008 and 2007, respectively. This increase is primary due to changes in our product mix, which have a shorter amortization period.

Federal Income Tax. We have a tax expense of $316,000 in 2008 on a pretax loss of $498,000. This is because the increase in fair value of warrants is not deductible for tax purposes. Without the $1.5 million change in warrant loss, the effective tax rate is 32.1%. The tax rate was low in 2007, due to the release of a tax valuation allowance of $1.2 million in the third quarter of 2007.

Nine Months Ended September 30, 2008 Compared to Nine Months Ended September 30, 2007

All comparisons below state the 2008 nine months first and the 2007 nine months second.

Consolidated Results of Operations

Net income for the nine months ended September 30, 2008 was $4.9 million, compared to $10.6 million for the same period of 2007. The primary cause of this variance was due to a decrease in income in the Home Service segment. This was caused by property losses incurred by SPFIC from Hurricanes Gustav and Ike, higher commissions, and higher death claims. Additionally, in the consolidated results of operations there was a loss from an increase in fair value of warrants associated with the Company s preferred stock.

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Total revenues were $123.4 million, a 2.1% increase over revenues of $120.9 million. Total revenues from our Life Insurance segment amounted to $85.1 million, compared to $81.4 million, reflecting continued strong renewal premium on the international business. Total revenues from Home Service decreased slightly to $38.6 million from $39.2 million.

Premium Income. Premium income increased to $101.9 million from $98.8 million, or 3.1%. The increase was attributable to persistency on the international business written in the Life Insurance segment, which had $72.6 million of premium income during the period. First year premiums in the Life Insurance segment during the first nine months of 2008 were down $1.9 million from comparable levels in 2007. This was primarily due to the slow production in the first quarter of 2008, as the international associates awaited the release of the new products. In the future, we expect our international sales production to reach or exceed the level achieved in 2007, as our new products gain additional popularity.

Net Investment Income. Net investment income increased 4.7% to $22.5 million, compared to $21.5 million, due primarily to the growth in our investment portfolio during 2008. Additionally, during 2007 and through the third quarter of 2008, we invested $60.7 million in equity mutual funds. We expect to keep equity mutual fund investments at about 10% of total invested assets to diversify our holdings and enhance potential returns. We continue to invest primarily in bonds of U.S. Government-sponsored enterprises, such as Fannie Mae and Freddie Mac.

Increase in Fair Value of Warrants. We incurred a loss on increase in fair value of warrants of $1.7 million in 2008 compared to a loss of $496,000 in 2007. The sizeable loss in 2008 was directly related to the increase in the price of our Class A common stock, as well as an increase in volatility. The warrant liability is calculated using the Black-Scholes option pricing model, which attempts to predict the value of the options when they expire in July 2011 and 2012. Current accounting standards require that the change in the value of the warrant liability is a component of revenues. When the liability goes up we incur a loss, and when the liability goes down we generate income. The warrant liability has no affect on the Company s cash flows, as the Company expects the warrants will be converted into our Class A common stock in July 2011, or sooner, at the election of the warrant holders, or expire.

Claims and Surrenders. As noted in the table below, claims and surrenders increased to $41.7 million from $37.9 million, due primarily to an increase in death and property claims and an increase in endowments.

	Nine Months Ended September 30,		
	2008		2007
	(In thousands)		
Death claims	$	17,058	16,152
Surrender benefits		10,768	10,154
Endowments		10,209	9,183
Property claims		2,226	649
Other policy benefits		1,146	1,498
Accident and health benefits		256	264
Total claims and surrenders	$	41,663	37,900

Death claims were up $906,000, comparatively, primarily due to a one-time 2007 period correction of an overstated prior year s claim liability of $650,000, which reduced 2007 death claim expense.

Surrenders were up $614,000 in 2008 as a result of the growth of insurance in force. Surrenders as a percent of ordinary whole life insurance were 0.3% of insurance in force in both 2008 and 2007.

Endowments were up 11.2%, or $1.0 million, as maturities within this block of policies have grown in recent years. The benefit is priced into the premium and does not have an adverse impact on results of operation.

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Property claims were up $1.6 million. Hurricanes Gustav and Ike swept through Louisiana during the third quarter of 2008, accounting for $635,000 of the increase. During the third quarter of 2007, we released reserves of $524,000 related to the 2005 hurricanes.

Policyholder Dividends. Policyholder dividends increased 5.9% to $4.6 million from $4.3 million, due to the continued sale and persistency of participating ordinary whole life products in the international market. All of our international policies are participating, and the growth of this block of business has contributed to the growth in dividends. The dividends are factored into the premiums and have minimal impact on profitability.

Change in Reserves. Reserves increased from $24.0 million in 2007 to $24.9 million in 2008 on an increase in life premium income of approximately $3.0 million.

Commissions. Commissions decreased to $25.9 million from $26.3 million in 2007, primarily due to the previously mentioned slowdown of new international policies issued in 2008. Offsetting a decrease in the Life Insurance segment commissions is an increase in Home Service commissions. Since conversion, Home Service commission calculations are manually estimated outside of the policy administration system based on growth of the in force annualized premium block. This estimation method has resulted in payment of commissions to agents in excess of the historical commissions during the nine months ended September 30, 2008 of approximately $1.0 million. The goal is to complete home service system enhancements by the end of 2008, which management believes will reflect commissions more in line with those paid prior to conversion.

Other Underwriting, Acquisition and Insurance Expenses. Expenses increased slightly to $21.2 million from $21.0 million, due primarily to an increase in salary expense, legal costs and international shipping, offset by a decrease in audit fees.

Deferred Policy Acquisition Costs. Capitalized deferred policy acquisition costs decreased 13.4% to $16.9 million from $19.5 million. This was a direct consequence of the reduction in new international business, as less commissions and expenses were capitalized. Amortization of these costs was $11.5 million and $9.5 million in 2008 and 2007, respectively. This increase is primarily due to changes in our product mix, which have a shorter amortization period.

Federal Income Tax. The effective tax rate for 2008 is 40.2%. If the non-deductible loss on the increase in the fair value of warrants is factored out, the effective tax rate is 33.4%. The effective tax rate for 2007 is 28.8%. This is low because a tax valuation allowance of $1.2 million was released in 2007, causing a reduction in tax expense.

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We are committed to the following contractual obligations as of September 30, 2008 with the payments due by the period indicated below:

Contractual Obligations	Total	Less than 1 Year	1 to 3 Years	3 to 5 Years	More than 5 Years
			(In thousands)		
Operating leases	$ 834	383	409	42	
Future policy benefit reserves:					
Life insurance	529,565	197	1,105	10,370	517,893
Annuities	24,394	12,761	5,719	2,466	3,448
Accident and health	7,485	7,485			
Total future policy benefit reserves	561,444	20,443	6,824	12,836	521,341
Policy claims payable:					
Life insurance	6,042	6,042			
Accident and health	949	949			
Property and casualty	2,180	2,180			
Total policy claims payable	9,171	9,171			
Convertible preferred stock	13,126		13,126		
Total contractual obligations	$ 584,575	$ 29,997	$ 20,359	$ 12,878	$ 521,341

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 in seeking to ensure stable and reliable sources of cash flows to meet obligations and is provided by a variety of sources.

Our liquidity requirements are met primarily by funds provided from operations. Premium revenues and deposits, 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 nine months of 2008, except bonds sold by SPFIC at a gain to fund hurricane claims.

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 renewed underwriting 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 $34.7 million and $22.1 million for the nine months ended September 30, 2008 and 2007, 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 $12.1 million and $33.6 million for the nine months ended September 30, 2008 and 2007, respectively. The outflows from investing activities for the nine months ended September 30, 2008 and 2007 primarily related to the investment of excess cash and cash equivalents generated from operations.

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Stockholders equity at September 30, 2008 was $164.9 million, compared to $176.2 million at December 31, 2007. The decrease in 2008 was largely due to income earned during the period of $4.9 million, offset by an increase in unrealized losses on investments of $19.2 million for the nine months ended September 30, 2008.

Investments decreased to $577.9 million at September 30, 2008 from $585.3 million at December 31, 2007, primarily because of the increase in unrealized losses. Fixed maturities are categorized into fixed maturities available-for-sale, which were 84.6% of investments at September 30, 2008 and 85.5% at December 31, 2007. Equity securities are categorized into equity securities available for sale, which are carried on our consolidated financial statements at fair value. Equity security investments were 8.2% of investments at September 30, 2008 and 6.1% at December 31, 2007.

The largest group of fixed maturities available-for-sale in a gross unrealized loss position for more than 12 months are primarily corporate and mortgage-backed securities acquired in the acquisition of Security Plan in 2004, and under purchase GAAP accounting, have a higher cost basis than historical cost. These premiums are being amortized to net investment income. Management has completed its assessment of other-than-temporary impairment of these securities. Based on our evaluation of the credit worthiness of the issuers and the Company s ability and intent to hold these securities to maturity, none of the unrealized losses are considered to be other-than-temporary.

The next largest group of fixed maturities available-for-sale in a gross unrealized loss situation for more than 12 months are investments in callable instruments issued by U.S. Government-sponsored enterprises and the current loss position primarily relates to changes in the current interest rate environment. Given the nature of the securities involved and the Company s intent and ability to hold these securities to full recovery, management does not believe that the unrealized losses on these instruments will result in realized losses.

Policy loans comprised 4.7% of invested assets at September 30, 2008 and 4.4% at December 31, 2007. These loans, which are secured by the underlying policy values, have annual yields ranging from 5% to 12% and maturities that are related to the maturity or termination of the applicable policies. Management believes that we maintain adequate liquidity despite the uncertain maturities of these loans.

Our cash balances at our primary depositories were significantly in excess of Federal Deposit Insurance Corporation coverage at September 30, 2008 and December 31, 2007. Management monitors the solvency of all financial institutions in which we have funds to minimize the exposure for loss. Management does not believe we are at significant risk for such a loss.

In the wake of bankruptcy filings by large corporations several years ago, concern was raised regarding the use of certain off-balance sheet special purpose entities such as partnerships to hedge or conceal losses related to investment activity. 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. We own no subprime or collateralized debt obligations.

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 an 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. At September 30, 2008 and December 31, 2007, all of our insurance subsidiaries were above required minimum levels.

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. 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.

At September 30, 2008 and December 31, 2007, GAAP reserve factors had not been developed by the consulting actuarial firm that calculates our GAAP reserves, post conversion, for all Security Plan paid-up policies. Because of this, reserves related to these policies were estimated based on the ratio of statutory reserves to GAAP reserves at September 30, 2007. This was the last time GAAP paid-up reserves were calculated by SPLIC s previous actuarial consulting firm.

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 does not exist at September 30, 2008. Management believes that our policy liabilities and increase in future policy benefit reserves as of and for the nine months ended September 30, 2008 and 2007 are based upon assumptions, including a provision for the risk of adverse deviation, that do not warrant revision. The relative stability of these assumptions and management s analysis is discussed below.

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 balance. 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.

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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.

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 as of and for the nine months ended September 30, 2008 and 2007 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.

Valuation of Investments in Fixed Maturity and Equity Securities

Our fixed maturities consist primarily of bonds. Fixed maturities that may be sold prior to maturity to support our investment strategies are considered held as available-for-sale and carried at fair value as of the balance sheet date. Equity securities (including non-redeemable preferred stock) are considered available-for-sale and are reported at fair value.

At September 30, 2008, 71.5% of our fixed maturity securities were invested in U.S. Government-sponsored enterprises or securities backed by the U.S. Government. We evaluate the carrying value of our fixed maturity and equity securities at least quarterly. A decline in the fair value of any fixed maturity or equity security below cost that is deemed other-than-temporary is charged to earnings resulting in the establishment of a new cost basis for the security. The new cost basis is not changed for subsequent recoveries in the fair value of the fixed maturity or equity security. With the exception of Security Plan, virtually all of our subsidiaries fixed maturity investments are in U.S. Government-sponsored enterprises or U.S. Government instruments. Security Plan has significant investments in corporate and municipal bonds. Management believes that our investments in fixed maturity securities at September 30, 2008 were not impaired, and no other-than-temporary losses needed to be recorded except a write down of one Lehman Brothers holding. This determination is based upon our holdings of fixed maturity securities, primarily obligations of U.S. Government-sponsored corporations, our intent and ability to hold temporarily impaired fixed maturities until recovery, and our analysis of whether declines in fair value below cost are temporary or other-than-temporary. Our equity securities consist of mutual funds acquired in 2008 and 2007, thus any declines in value are recent and are currently considered temporary. We will continue to monitor these investments. At September 30, 2008, there were no other-than-temporary impairments on equity securities.

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 primary annuity products do not include fees or other such charges.

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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.

Market Risk Related to Interest Rates

Our exposure to interest rate changes results from our significant holdings of fixed maturity investments, which comprised over 84.6% of our investment portfolio as of September 30, 2008. 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 71.5% of the fixed maturities we owned at September 30, 2008 are instruments of U.S. Government-sponsored enterprises, or are 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 100 basis point shifts in the prevailing interest rates.

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 decreased slightly to 3.8% during the quarter ended September 30, 2008 from 4%, at December 31, 2007. Also during the quarter, the world economy struggled through the credit crisis, with many large banks and financial intuitions writing off large amounts of bad investments or filing for bankruptcy. This current financial crisis caused our unrealized losses to increase to $21.3 million for the quarter ended September 30, 2008, on a portfolio of $577.9 million. This primarily relates to our holdings of fixed maturities and equity securities.

We preformed a sensitivity analysis, as of December 31, 2007, for our interest rate-sensitive assets. The changes in market values of our debt and equity securities as of September 30, 2008 were within the expected range of results of this analysis.

There are no fixed maturities or other investments that we classify as trading instruments. Recent news has focused on sub prime assets, collateralized debt obligations, and risky mortgage backed investments. The Company does not have any exposure to these investments. With over 71.5% of our fixed maturities invested in the U.S. Government or U.S. Government sponsored-enterprises, the Company s portfolio is well positioned for the current credit crisis.

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. However, our equity investments portfolio was less than 10% of our total investments at September 30, 2008. Thus, we believe that significant decreases in the equity markets would not have a material adverse impact on our total investment portfolio.

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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 (CEO) and Chief Financial Officer (CFO) 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 annual report.

During the quarter ended September 30, 2008 there have been no changes in the Company s internal controls over financial reporting that materially affect or are reasonably likely to effect, the Company s internal controls over financial reporting (as defined in rules 13a-15(f) and 15d-15(f) under the Exchange Act).

During the second quarter the Company implemented an internal audit function. The internal audit function will provide an additional layer of controls and review procedures. The Company s new director of internal audit has significant experience in the life insurance industry, as well as external audit experience including design and implementation of SOX processes.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are a defendant in a lawsuit originally filed on August 6, 1999 in the Texas District Court, Austin, Texas, now styled *Citizens Insurance Company of America, Citizens, Inc., Harold E. Riley and Mark A. Oliver, Petitioners v. Fernando Hakim Daccach*, *Respondent*, in which a class was originally certified by the trial court and affirmed by the Court of Appeals for the Third District of Texas. We appealed the grant of class status to the Texas Supreme Court, which on March 2, 2007, reversed the Court of Appeal s affirmation of the trial court s class certification order, decertified the class and remanded the case to the trial court for further proceedings consistent with the Texas Supreme Court s opinion. As a result, no class action is presently certified, and plaintiffs counsel is seeking to recertify the class. In order to recertify the class, the lead plaintiff must establish that he is qualified to represent the purported class and that the res judicata effect of a class action will not have a deleterious effect on the putative class members. The underlying lawsuit alleges that certain life insurance policies that we 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. We believe the lawsuit is without merit and intend to continue a vigorous defense in any remaining proceedings, including any class recertification. If the class is recertified, we could be exposed to costly and time-consuming litigation, and an adverse judgment could have a material adverse effect on our results of operations and financial condition. The case is now before the District Court judge for an analysis of the evidence presented to determine if it warrants recertification of a class.

SPFIC is a defendant in a suit styled *The State of Louisiana v. AAA Insurance*, or *Road Home Litigation*, which was filed in the Civil District Court for the Parish of Orleans on August 23, 2007 by the state of Louisiana as subrogee/assignee of the insureds of more than 200 different insurance companies. The suit was filed to recover money that the state of Louisiana paid to certain insureds under the Louisiana Road Home Program for damages resulting from Hurricanes Katrina and Rita. The suit was removed to the United States District Court for the Eastern District of Louisiana on September 11, 2007 and appeals of the removal have been denied. Responsive pleadings have not yet been filed on behalf of any of the defendant insurers in this case, nor has any discovery been conducted to date.

SPFIC was also named as a defendant in a lawsuit filed in the Civil District Court for the Parish of Orleans on behalf of Karen Cheneau in August 2006. The *Cheneau* suit stems from damages Ms. Cheneau sustained during Hurricane Katrina. In November 2007, plaintiff filed a Motion for Leave to File First Amended Petition to Assert Class Allegations against SPFIC. The purported class consists of Louisiana citizens who purchased homeowner s insurance coverage and/or contents insurance coverage from SPFIC, whose homes and/or property covered by said policies were damaged as a result of Hurricane Katrina and who timely submitted claims to SPFIC for their losses, and who either received no recovery or received less than the alleged proper value of their valued policies as a result of their claims. SPFIC has responded to the Amended Petition by filing Exceptions of No Cause of Action, No Right of Action, Vagueness, Prescription and Failure to Meet Class Action Requirements. In April 2008, the Plaintiff s local counsel in Louisiana filed an Ex Parte Motion to Withdraw from the case. Currently, the Plaintiffs are without local counsel to file pleadings and attend hearings on their behalf. The Exceptions have not yet been set for hearing. SPFIC intends to vigorously defend this lawsuit.

The *Road Home Litigation* and *Cheneau* are in the early stages of litigation, and no discovery has yet occurred. Therefore, it is not possible to evaluate how many claims in those cases relate to SPFIC, or the potential exposure to SPFIC. However, in the event of an adverse outcome, the potential exposure to SPFIC could be significant.

On November 8, 2005, SPLIC was named as a defendant in a suit styled *Lilac Todd vs. Security Plan Life Insurance Company*, on behalf of Lilac Todd, which alleges that SPLIC failed to pay Ms. Todd s claim for medical expenses arising out of the loss of one of her limbs. On December 20, 2007, a Supplemental and Amended Petition for Damages was filed pursuant to which the plaintiff has asserted class action allegations. The purported class is defined as all Louisiana insureds of SPLIC whose policies contained an incontestability provision identical or similar to Ms. Todd s policy, and whose claims were denied within 10 years of the petition filing on the basis of illnesses, injuries or diseases diagnosed or which occurred at any time preceding the incontestability.

This matter is in the early stages of litigation relative to the class allegations. Plaintiffs have not established how many, if any, individuals are within the class definition proposed by plaintiff. SPLIC intends to aggressively defend this action. However, in the event of an adverse outcome, the potential exposure to SPLIC could be significant.

In addition to the legal proceedings 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. We have not established any reserve account on our consolidated financial statements for the adverse financial impact of any of our litigation matters.

ITEM 1A. RISK FACTORS

The following risk factors supplement the risk factor disclosure in our Annual Report on Form 10-K for the Year Ended December 31, 2007.

Lack of market acceptance of our new insurance policies for our non-U.S. residents could negatively impact our financial results.

We are in the midst of introducing new insurance policies for non-U.S. residents. Our new production of insurance from non-U.S. residents slowed in the nine months of 2008 due to our marketing force s familiarity than anticipated acceptance of these new policies. Also, disruption in some of our key markets, both regulatory and internal within marketing structures, further slowed sales during the first nine months. If our foreign independent marketing consultants and marketing firms are not able to achieve sales of the new policies consistent with past levels of policy sales, we may be faced with a decrease in the number of these consultants and marketing firms, which would hinder our growth objectives. In addition, continued disruption of our foreign independent marketing consultants and marketing firms would reduce our new insurance policy sales significantly and have a material adverse effect on our results of operations and financial conditions.

Success of our business depends in part on effective information technology systems and on continuing development and implementation of improvements.

Our business is dependent upon the ability to keep up to date with effective, secure and advanced technology systems for the integration of the policy administration, accounting, and investment systems. It is crucial to our business to service a large number of policyholders, provide timely and accurate information, and do so in a technology system that is secure. If we do not maintain adequate systems adaptable to technological advancements, adverse consequences could include inadequate information on which to base pricing, underwriting and reserving decisions, regulatory complications, litigation exposure or increases in administrative expenses. This could adversely affect our ability to service policyholders and make attracting new customers difficult.

Some of our information technology systems and software are mainframe-based, legacy-type systems and require an ongoing commitment of resources to maintain current standards. We continuously enhance and update our systems to keep pace with changes in our products and business models, information processing technology, evolving industry and regulatory standards and policyholder needs. Our success is in large part dependent on maintaining and enhancing the effectiveness of existing systems, as well as continuing to integrate, develop and enhance our information systems to support business processes in a cost-effective manner.

We are experiencing a delay in the completion of the conversion of Security Plan s Home Service administration system to our policy administration system.

At December 31, 2007, the Security Plan in force policies were transitioned to the Company s integrated policy administration system and Security Plan s original computer system was eliminated for production purposes and continues to be available only for historical information inquiry. The conversion was successful and all in force amounts were reconciled between systems. The Company recognized, due to the uniqueness of home service business, that some actuarial estimates would be necessary on an interim basis until the home service administrative modifications and enhancements are completed later in 2008.

Although we plan to complete all modifications related to home service administration by the end of the 2008, we cannot assure this project will be completed by then. In addition, in working through these issues we could identify other required modifications or changes which will take precedence over these. If any of the items above or any other unforeseen issues emerge during the integration process, they could have a material or significant impact on our financial results in 2008.

Gross Unrealized Losses May be Realized or Result in Future Impairments.

Our gross unrealized losses on our securities portfolio at September 30, 2008 were $21.3 million pre-tax compared to $2.1 million pre-tax at December 31, 2007. While we intend to hold these instruments to maturity, realized losses or impairments on them may have a material adverse impact on our results of operation and financial position.

Adverse capital and credit market conditions may significantly affect our access to debt and equity capital and our cost of capital in seeking to expand our business.

The capital and credit markets have been experiencing extreme volatility and disruption for over a year. In recent months, the volatility and disruption reached unprecedented levels. In some cases, the markets exerted downward pressure on availability of debt and equity capital for certain issuers, including short term liquidity and credit capacity. The availability of equity and debt financing to us will depend on a variety of factors such as market conditions, the general availability of credit, the overall availability of credit to the financial services industry, our credit capacity, as well as the possibility that investors or lenders could develop a negative perception of our long- or short-term financial prospects. Disruptions, uncertainty or volatility in the capital markets may also limit our access to equity capital for us to seek to expand our business. As such, we may be forced to delay raising capital, or bear an unattractive cost of capital which could decrease our profitability.

Difficult conditions in the global capital markets and the world economy generally may materially adversely affect our business and results of operations and we do not expect these conditions to improve in the near future

Our results of operations are materially affected by conditions in the economy generally, both in the U.S. and elsewhere around the world. The stress experienced by global capital markets that began in the second half of 2007 continued and substantially increased during the third quarter of 2008. Recently, concerns over inflation, energy costs, geopolitical issues, the availability and cost of credit, the U.S. mortgage market and a declining real estate market in the U.S. have contributed to increased volatility and diminished expectations for the world economy and the equity and debt markets going forward. These factors, combined with volatile commodity prices, declining business and consumer confidence and increased unemployment, have precipitated a global recession. As a result, domestic and international equity markets have been experiencing heightened volatility and turmoil, with issuers in the financial services industry particularly affected. These events and the continuing market upheavals may have an adverse effect on us, in part because we are dependent upon customer behavior. Our revenues could decline in such circumstances and our profit margins could erode, although through the third quarter of this year we have not experienced significant revenue declines compared to prior periods. However, our production of new insurance business has slowed compared to 2007.

Factors such as consumer spending, business investment, government spending, the volatility and strength of the capital markets, and inflation all affect the business and economic environment and, ultimately, the amount and profitability of our business. In an economic downturn characterized by higher unemployment, lower personal incomes, lower corporate earnings, lower business investment and lower consumer spending, the demand for our insurance products could be adversely affected. In addition, we may experience an elevated incidence of lapses or surrenders of our insurance policies. Our policyholders may choose to defer paying insurance premiums or stop paying insurance premiums altogether. Adverse changes in the global economy could therefore affect earnings negatively and could have a material adverse effect on our business, results of operations and financial condition.

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There can be no assurance that actions of the U.S. Government ,the Federal Reserve and other governmental and regulatory bodies for the purpose of stabilizing the financial markets will achieve the intended effect

In response to the financial crises affecting the U.S. banking system and financial markets and going concern threats to investment banks and other financial institutions, on October 3, 2008, President Bush signed the Emergency Economic Stabilization Act of 2008 (the EESA) into law. Pursuant to the EESA, the U.S. Treasury has the authority to, among other things, purchase up to $700 billion of mortgage-backed and other securities from financial institutions for the purpose of stabilizing the financial markets and invest in financial services companies. The Federal Government, the Federal Reserve and other governmental and regulatory bodies have taken or are considering taking other actions to address the current financial crisis, including purchases of commercial paper. There can be no assurance as to what impact such actions will have on the financial markets, including the high levels of volatility currently being experienced. Such continued volatility could materially and adversely affect our business, financial condition and results of operations, or the trading price of our Class A common stock.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4.

None.

ITEM 5. OTHER INFORMATION

None.

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)

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Exhibit Number	The following exhibits are filed herewith:
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)
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)
10.6	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)
11	Statement re: Computation of per share earnings (see financial statements)
21	Subsidiaries of Registrant (k)
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*

* **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.

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(b) Filed 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.

(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. I, 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 March 30, 2007 with the Registrant s Annual Report on Form 10-K for the Year Ended December 31, 2006 as Exhibit 21, 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/ Thomas F. Kopetic
Thomas F. Kopetic
Vice President, Chief Financial Officer
and Treasurer

Date: November 7, 2008

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EXHIBIT INDEX

Exhibit Number	Description
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
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