CITIZENS FINANCIAL CORP /KY/
Form 10-K
April 07, 2003

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U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

X ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended DECEMBER 31, 2002
or
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission file number 0-20148

CITIZENS FINANCIAL CORPORATION
(Exact name of registrant as specified in its charter)

Kentucky	61-1187135
(State of Incorporation)	(I.R.S. Employer Identification No.)

12910 Shelbyville Road, Louisville, Kentucky 40243
(Address of principal executive offices)

(502) 244-2420
(Registrant's telephone number)

Securities registered pursuant to Section 12(b) of the Act:
None

Securities registered pursuant to Section 12(g) of the Act:
Class A Stock, No Par Value

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, and (2) has been subject to such filing requirements for the past 90 days. Yes ~~X~~ No ~~~~~

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [~X~]

Indicate by check mark whether the registrant is an accelerated filer (as determined in Rule 12b-2 of the Securities Exchange Act of 1934). Yes ~~~~~ No ~~X~~

State the aggregate market value of the common equity held by non-affiliates of the registrant: $3,055,495 (based on an $4.77 per share average of bid and asked prices on March 25, 2003).

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date: 1,685,228 shares of Class A

Stock as of March 25, 2003.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the issuer's Board of Director's Proxy Statement for the Annual Meeting of Shareholders now scheduled for May 22, 2003 are incorporated into Part III of this Form 10-K. The date of this Report is April 7, 2003.

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This report contains projections and other forward-looking statements regarding future events or the future financial performance of the Company. Actual events and results may differ materially from those in the projections and other forward-looking statements set forth herein. Among the important factors that

could cause actual events or results to differ materially from those in the projections and other forward-looking statements are: changes in the market value of the Company's investments, including stock market performance and interest rate changes; customer response to marketing efforts; mortality and morbidity trends; regulatory changes; actions of independent rating agencies; general economic conditions and increased competition; the Company's ability to achieve operating efficiencies; unanticipated adverse litigation; and changes in Federal tax law. Readers are referred to the Items 1, 7, 7a and 8 in this report and to the Company Report on Financial Statements in the Company's Annual Report for a discussion of these and other important risk factors concerning the Company and its operations.

PART I
ITEM 1. BUSINESS

General

Citizens Financial Corporation (herein, the "Company" or the "Registrant") was incorporated in Kentucky in 1990 at the direction of the Board of Directors of Citizens Security Life Insurance Company ("Citizens Security") for the ultimate purpose of becoming an insurance holding company. Pursuant to a merger completed in 1991, Citizens Security became a wholly owned subsidiary of the Company. The Company is now a holding company that engages in the business of life insurance, annuities, and accident and health insurance through Citizens Security and United Liberty Life Insurance Company ("United Liberty") (herein collectively, the "Life Insurance Subsidiaries"). The Company also owns Citizens Insurance Company ("Citizens Insurance"), which is licensed as a property and casualty insurer but currently has no business inforce. The Life Insurance Subsidiaries and Citizens Insurance are herein collectively referred to as the "Insurance Subsidiaries".

Citizens Security was incorporated in Kentucky and commenced business in 1965. In 1971, Citizens Security acquired Central Investors Life Insurance Company by merger. In 1987, it purchased the stock of Old South Life Insurance Company ("Old South"). In 1992, Old South merged into Citizens Security. In 1995, the Company and Citizens Security purchased all of the stock of Integrity National Life Insurance Company ("Integrity") and merged it into Citizens Security. During May 1998, Citizens Security purchased all of the outstanding shares of United Liberty. In October 1999, the Company acquired Citizens Insurance and in January 2001, it contributed the stock of Citizens Insurance to Citizens Security. See Item 7 and Note 2 of the Notes to Consolidated Financial Statements, for descriptions of certain of these acquisitions. The Life Insurance Subsidiaries are currently licensed to transact the business of life insurance, annuities, and accident and health insurance. Citizens Security is licensed in twenty states and the District of Columbia while United Liberty is licensed in twenty-three states and Citizens Insurance is licensed in six states.

Insurance Operations

The Company, through its Life Insurance Subsidiaries, operates in five segments -- 1) home service life insurance, 2) broker-sold life insurance and annuities, 3) preneed life insurance, 4) dental insurance, and 5) other health and accident insurance. The home service and preneed life segments provide individual coverages; the dental segment provides group coverages; while the broker life and other health segments include individual and group insurance coverages. The following table presents each business segment"s revenue; pretax income or loss

excluding realized investment gains and interest expense; and ending assets for each of the last three fiscal years. Additional segment information is contained in Item 7 and in Note 9 of the Notes to Consolidated Financial Statements.

Segment Revenue, Profit or Loss, and Assets:

December 31	2002	2001	
Revenue:			
Home Service Life	$ 9,260,097	$ 9,290,120	$ 9
Broker Life	5,964,089	6,497,286	6
Preneed Life	19,706,136	9,974,405	5
Dental	8,209,257	8,025,375	7
Other Health	1,432,607	1,487,562	1
Segment Totals	44,572,186	35,274,748	30
Net realized investment gains (losses)	(2,469,768)	(7,911,829)	1
Total Revenue	$ 42,102,418	$ 27,362,919	$ 31

Year Ended December 31	2002	2001	
Segment Profit (Loss):			
Home Service Life	$275,809	$ 382,723	$
Broker Life	(265,488)	74,960	
Preneed Life	(670,349)	(264,488)	
Dental	297,740	256,385	
Other Health	(191,289)	10,847	
Segment Totals	(553,577)	460,427	
Net realized investment gains (losses)	(2,469,768)	(7,911,829)	1
Interest expense	305,715	532,962	
Income (Loss) before income tax and cumulative effect of a change in accounting principle	$ (3,329,060)	$ (7,984,364)	$

December 31	2002	2001	
Assets:			
Home Service Life	$ 45,219,971	$ 44,818,038	$ 45
Broker Life	53,874,949	54,954,194	57
Preneed Life	46,739,831	34,138,535	29
Dental	660,334	726,728	
Other Health	1,946,447	1,959,588	2
Total Assets	$148,441,532	$136,597,083	$135

Home Service Life. The Home Service Life segment consists primarily of

traditional whole life insurance, which provides policyholders with permanent life insurance and fixed, guaranteed rates of return on the cash value element of policy premiums. Agents for these products sell primarily small face value policies (typically from $1,000 to $10,000). These policies are subject to normal underwriting procedures with the extent of such procedures determined by the amount of insurance, age of applicant and other pertinent factors.

Broker Life. The Broker Life segment offers traditional whole life insurance; universal life insurance, which provides policyholders with permanent life insurance and adjustable rates of return on the cash value element of policy premiums, based upon current interest rates; annuities; group life; accidental death and dismemberment; and dependent life insurance. The majority of Broker Life sales consist of whole life graded death benefit and simplified issue policies.

The graded death benefit policy returns premium plus interest compounded at an annual rate of 10% if the insured dies of natural causes during the first three years the policy is in force. If the insured dies of an accidental cause, the benefit payable is the face amount of the policy. The simplified issue product provides full face amount coverage from date of issue, is more extensively underwritten and carries lower premium rates than the graded death benefit product. These products are targeted towards the "final expense market".

Generally, traditional whole life insurance products are more profitable than universal life policies, in part because investment margins are normally greater for traditional whole life products than for universal life policies. Overall profitability on universal life policies may decline as a result of downward interest crediting rate adjustments to the extent that policyholders withdraw funds to invest in higher-yielding financial products. The profitability of traditional whole life products and universal life policies is also dependent upon the ultimate underwriting experience and the realization of anticipated unit administrative costs. The Company believes that the historical claims experience for the traditional whole life and universal life products issued by the Life Insurance Subsidiaries has been within expected ranges, in relation to the mortality assumptions used to price the products.

Substantially all annuity considerations are attributable to sales of flexible premium deferred annuities, life policy annuity riders, and single premium deferred annuities. Generally, a flexible premium deferred annuity or a life policy annuity rider permits premium payments in such amounts as the policyholder deems appropriate, while a single premium deferred annuity requires a one-time lump sum payment.

Preneed Life. The Preneed Life segment products are traditional whole life policies sold to individuals in connection with prearrangement of their funeral and include single and multi-pay coverages, generally in amounts of $10,000 and less. These policies are generally sold to older individuals at increased premium rates.

The following table provides information concerning the Life Insurance Subsidiaries' volume of life insurance coverage in force excluding participation in group underwriting pools for federal employees (FEGLI) and service personnel (SGLI) for each of the last three fiscal years.

Year Ended December 31 (Dollars in Thousands)	2002	2001
Gross In-force at beginning of period1	$812,515	$809,045
Business purchased	---	---
New business issued during period:		

Individual	$95,706	$ 113,119
Group	13,063	7,632
New business total	$108,769	$ 120,751
Terminations during period	$128,562	$ 117,281
Termination rate2	15.8%	14.5%
Gross In-force at end of period1:		
Individual	$663,394	$668,565
Group	129,328	143,950
Gross In-force total at end of period	$792,722	$812,515
Reinsurance ceded at end of period	96,202	109,227
Net In-force at end of period	$696,520	$703,288

Dental Insurance. Dental products are indemnity policies sold on a pure group and voluntary group basis. Voluntary dental groups must meet prescribed participation limits. All dental products have annual limits on all covered procedures and lifetime limits on orthodontia procedures. In addition, orthodontia and major restorative procedures are not covered for the first six months to one year, depending upon the plan, unless a no-loss-no-gain provision is attached to the policy.

Other Health Insurance. Other Health products include individual accident and health insurance policies, which provide coverage for monthly income during periods of hospitalization, scheduled reimbursement for specific hospital and surgical expenses and cancer treatments, and lump sum payments for accidental death or dismemberment. Group health plans are also offered, providing coverage for short-term disability, and income protection. The Company is not allocating significant marketing resources to this segment.

Marketing. The Life Insurance Subsidiaries are currently licensed to sell products in 29 states and the District of Columbia. Citizens Security and United Liberty are both licensed in the states designated below with a "b" while only Citizens Security is licensed in the states designated "c" and only United Liberty in the states designated "u".

b Alabama	b Indiana	u Nebraska	u Oregon
u Arizona	u Kansas	u Nevada	c Pennsylvania
b Arkansas	b Kentucky	c New Jersey	b South Carolina
u Colorado	b Louisiana	u New Mexico	b Tennessee
c Delaware	b Maryland	c North Carolina	b Texas
c District of Columbia	b Mississippi	u Oklahoma	u Utah
b Florida	b Missouri	b Ohio	c Virginia
c Georgia			b West Virginia

The Life Insurance Subsidiaries market products through the personal producing general agent distribution system. Approximately 3,500 sales representatives are licensed as independent agents for the Life Insurance Subsidiaries. The majority of these agents also represent other insurers. Approximately 600 of these agents specialize in the home service market. That market consists primarily of middle and low-income families and individuals who desire whole life policies with policy limits typically below $10,000. Agents usually collect premiums directly at monthly intervals. The home service market has higher than average policy

lapse rates. Approximately 800 agents specialize in the preneed market. Typically, these agents are funeral directors or operate from facilities owned by funeral directors.

The Life Insurance Subsidiaries furnish rate material, brochures, applications, and other pertinent sales material, at no expense to the agents. The agents are responsible for complying with state licensing laws and any related appointment fees. Agents are compensated by commissions. The Life Insurance Subsidiaries have agent commission arrangements that are generally intended to provide competitive incentives for agents to increase their production of new insurance and to promote continued renewals of in-force insurance. Historically, these incentives have frequently involved awards, overrides, and compensation scales that escalate according to achievement levels for newly-issued business and that provide additional payments for renewal business.

Underwriting. The Life Insurance Subsidiaries follow underwriting procedures designed to assess and quantify insurance risks before issuing life and health insurance policies to individuals and members of groups. Such procedures require medical examinations (including blood tests, where permitted) of applicants for certain policies of health insurance and for policies of life insurance in excess of certain policy limits. These requirements are graduated according to the applicant's age and vary by policy type. In addition, certain types of life insurance policies are offered with higher premium rates and less stringent underwriting requirements. The Life Insurance Subsidiaries also rely upon each applicant's written application for insurance, which is generally prepared under the supervision of a trained agent. In issuing health insurance, information from the application and, in some cases, inspection reports, physician statements, or medical examinations are used to determine whether a policy should be issued as applied for, issued with reduced coverage under a health rider, or rejected.

Acquired Immunodeficiency Syndrome ("AIDS") claims identified to date, as a percentage of total claims, have not been significant for the Life Insurance Subsidiaries. Evaluating the impact of future AIDS claims under health and life insurance policies issued is extremely difficult, in part due to the insufficiency and conflicting data regarding the number of persons now infected with the AIDS virus, uncertainty as to the speed at which the AIDS virus has and

may spread through the general population, and advancements in medical treatment options. The Life Insurance Subsidiaries have implemented, where legally permitted, underwriting procedures designed to assist in the detection of the AIDS virus in applicants.

Investments. The Company derives a substantial portion of its revenue from investments. The Life Insurance Subsidiaries maintain diversified investment portfolios that are held primarily to fund future policyholder obligations. State insurance laws impose certain restrictions on the nature and extent of investments by insurance companies and, in some states, require divestiture of assets contravening these restrictions. Within the framework of such laws, the Life Insurance Subsidiaries follow a general strategy to maximize total return (current income plus appreciation) without subjecting themselves to undue risk. Where deemed appropriate, the Life Insurance Subsidiaries will hold selected non-investment grade bonds that provide higher yields or are convertible to common stock. The Company considers a bond non-investment grade if it is unrated or rated less than BBB by Standard & Poor's Rating Group ("S&P") or BAA by Moody's Investors Service ("Moody's"). The Company's non-investment grade bonds, based on reported fair values, represented 4.1% of the Company's cash and invested assets as of December 31, 2002. Citizens Security has maintained substantial investments in equity securities in order to achieve higher investment earnings than can usually be achieved through portfolio bonds but at

a greater comparative risk. The Company also maintains an investment portfolio of equity securities separate from those of the Insurance Subsidiaries. Mortgage loans, federally-insured mortgage-backed securities, collateralized mortgage obligations and real estate investments, apart from the investment in the office building described in Item 2. "Description of Property," represented approximately 8.0% of cash and invested assets as of December 31, 2002. Neither the Company nor its subsidiaries owned any collateralized mortgage-backed securities as of December 31, 2002 that would be included in the high-risk classification.

For additional information concerning investment results, see Item 7.

Reinsurance. In keeping with industry practice, the Life Insurance Subsidiaries reinsure, with unaffiliated insurance companies, portions of the life and health insurance risks which they underwrite. The Life Insurance Subsidiaries retain no more than $40,000 of individual life insurance risk and $15,000 of group life insurance risk for any single life. Graded death benefit and simplified issue coverages above $4,000 are generally 50% reinsured, with the Life Insurance Subsidiaries maintaining a maximum $10,000 risk on any one life. Individual and group accidental death coverage is 100% reinsured. At December 31, 2002, approximately $96,202,000 or 12% of life insurance in force was reinsured under arrangements described in Note 11 of the Notes to the Consolidated Financial Statements. Under most reinsurance arrangements described above, new insurance is reinsured automatically rather than on a basis that would require the reinsurer's prior approval. Generally, the Life Insurance Subsidiaries enter into indemnity reinsurance arrangements to assist in diversifying their risks and to limit their maximum loss on large or unusually hazardous risks. Indemnity reinsurance does not discharge the ceding insurer's liability to meet policy claims on the reinsured business. Accordingly, the Life Insurance Subsidiaries remain responsible for policy claims on the reinsured business to the extent a reinsurer should fail to pay such claims.

Competition. The insurance industry is highly competitive, with approximately 1,500 life and health insurance companies in the United States. Many insurers and insurance holding company systems have substantially greater capital and surplus, larger and more diversified portfolios of life and health insurance policies, and larger agency sales operations than those of the Life Insurance Subsidiaries. Financial and claims-paying ratings assigned to insurers by A.M. Best Company ("Best") and by nationally-recognized statistical rating organizations have become more important to policyholders. Citizens Security's rating was last changed by Best in October, 2001, when it was downgraded to B- (Fair) from B (Fair). United Liberty's rating has remained at B- (Fair) since its 1998 acquisition. According to Best, B- ratings are assigned to companies that have on balance, fair financial strength, operating performance and market profile when compared to the standards established by Best. Also according to Best, B- companies have an ability to meet their current obligations to policyholders, but their financial strength is vulnerable to adverse changes in underwriting or economic conditions. There are seven Best rating categories above the B- category from B to A++. The Life Insurance Subsidiaries will continue to pursue upward revisions in their Best ratings. Citizens Insurance has no insurance business inforce and is not rated by Best.

S&P assigns claims-paying ability ratings to certain U.S. insurers. Generally, such a rating is S&P's opinion of an insurer's financial capacity to meet the obligations of its insurance policies in accordance with their terms. In the case of companies like Citizens Security that have not requested ratings, S&P's methodology uses statistical tests based on statutory financial data as filed with the National Association of Insurance Commissioners ("NAIC"). The rating process does not involve contact between S&P analysts and the insurer's management. In 1998, S&P changed its rating methodology and revised Citizens Security's rating from BBq to BBpi. (The "q" subscript designated the quantitative method of rating while the "pi" subscript designates the public

information method). United Liberty has not been rated by S&P. According to S&P,

BB companies may have adequate financial security but their capacity to meet policyholder obligations is vulnerable to adverse economic and underwriting conditions. The BB rating is the highest of five ratings in the vulnerable range of ratings.

A rating is not a recommendation to buy, sell or hold securities and is subject to revision or withdrawal by the assigning rating organization. Each rating should be evaluated independently of any other rating.

The Life Insurance Subsidiaries compete primarily on the basis of the experience, size, accessibility and claims response of their customer service representatives, product design, service and pricing. The Company believes that the Life Insurance Subsidiaries are generally competitive in the markets in which they are engaged based upon premium rates and services, have good relationships with their agents, and have an adequate variety of insurance and annuity products approved for issuance.

State Insurance Regulation. The Insurance Subsidiaries, in common with other insurers, are subject to comprehensive regulation in the states in which they are authorized to conduct business. The laws of such states establish supervisory agencies with broad administrative powers, among other things, to grant and revoke licenses for transacting business, regulate the form and content of policies, establish reserve requirements, prescribe the type and amount of allowable investments, and review premium rates for fairness and adequacy. The Insurance Subsidiaries file detailed annual statements with all states in which they are licensed to transact business. The Kentucky Department of Insurance also periodically examines the business and accounts of the Insurance Subsidiaries. In recent years, various state insurance departments and the NAIC have expressed concern, essentially about the "rate of return" earned by holders of small face amount life policies, potentially including Preneed policies. Although the Company does not believe calculating a simple "rate of return" is meaningful for traditional life insurance products, state insurance regulators could take steps that would alter the profitability of existing policies and/or eliminate small face amount policies as a viable product offering.

The Life Insurance Subsidiaries also can be required, under the solvency or guaranty laws of most states in which they do business, to pay assessments (up to prescribed limits) to fund policyholder losses or liabilities of other insurance companies that become insolvent. These assessments may be deferred or foregone under most guaranty laws if they would threaten an insurer's financial strength and, in certain instances, may be offset against future premium or intangible property taxes. Gross assessments for the Life Insurance Subsidiaries, net of (refunds) but before offsets for future premium or intangible property taxes, were $12,587, $(1,000), and $(11,000) in 2002, 2001, and 2000, respectively.

Kentucky, in common with substantially all states, regulates transactions between or affecting insurance holding companies and their insurance company subsidiaries, including the Company and the Insurance Subsidiaries. Generally, under Kentucky insurance holding company statutes, the Kentucky Department of Insurance must approve in advance the direct or indirect acquisition of 15% or more of the voting securities of an insurance company organized under the laws of Kentucky. Such statutes also regulate certain transactions among affiliates, including the payment of dividends by an insurance company to its holding company parent. Under the Kentucky statutes, the Insurance Subsidiaries may not during any year pay dividends on their common and preferred stock to their parent company in excess of the lesser of the net gain from operations for the

preceding year or 10% of their capital and surplus at the end of the preceding year, without the consent of the Kentucky Commissioner of Insurance. For 2003, the maximum amount of dividends that United Liberty and Citizens Insurance could pay, without the Commissioner's approval, is $215,000, and $62,000 respectively. Citizens Security is unable to pay such a dividend. The Company provides substantially all management, operating and employee services for the Insurance Subsidiaries and is reimbursed at actual cost plus fifteen percent. This management fee totaled $4,704,000 for 2002. The Company currently has resources which could be adequate to service debt obligations through 2004. In addition, the Company's Chairman has expressed potential willingness to lend up to $3,000,000 of additional funds to the Company if necessary. Accordingly, the Company is not relying upon affiliate dividends or preferred stock redemptions for near-term debt service.

During recent years, the National Association of Insurance Commissioners (NAIC) has taken several steps to address public concerns regarding insurer solvency. These steps included implementing a state certification program designed to promote uniformity among the insurance laws of the various states and developing insurer reporting requirements that focus on asset quality, capital adequacy, profitability, asset/liability matching, and liquidity. These requirements include establishment of asset valuation reserves ("AVR") and interest maintenance reserves ("IMR"), risk-based capital ("RBC") rules to assess the capital adequacy of an insurer, and a revision to the Standard Valuation Law ("SVL") that specifies minimum reserve levels and requires cash flow testing in

which projected cash inflows from assets are compared to projected cash outflows for liabilities to determine reserve adequacy.

The Life Insurance Subsidiaries' AVR, as of December 31, 2002, 2001 and 2000, is shown in Item 7. Cash flow testing and the results of such testing as applied to the Life Insurance Subsidiaries are also described and discussed in Item 7.

RBC provides a means of establishing the capital standards for insurance companies to support their overall business operations in light of their size and risk profile. The four categories of major risk involved in the formula are [i]asset risk -- the risk with respect to the insurer's assets; [ii]insurance risk -- the risk of adverse insurance experience with respect to the insurer's liabilities and obligations; [iii]interest rate risk -- the interest risk with respect to the insurer's business; and [iv]business risk -- all other business risks. A company's RBC is calculated by applying factors to various asset, premium and reserve items, with higher factors for those items with greater underlying risk and lower for less risky items. RBC standards are used by regulators to set in motion appropriate regulatory actions relating to insurers that show signs of weak or deteriorating conditions. They also provide an additional standard for minimum capital, below which companies would be placed in conservatorship.

Based on RBC computations as of December 31, 2002, the Insurance Subsidiaries each have capital which is well in excess minimum regulatory requirements.

Action taken by the NAIC in these and other areas may have a significant impact on the regulation of insurance companies during the next several years. In addition, various proposals are being considered for permitting insurers to elect Federal regulation. Given their comparatively small size, it may be expected that the Life Insurance Subsidiaries would be affected by more stringent regulatory policy, both under existing laws and any new regulatory initiatives. Such effects could include curtailment or discontinuance of insurance underwriting in one or more states, mandated increases in capital and surplus, and/or other effects.

Income Taxation. The Life Insurance Subsidiaries are taxed under the life insurance company provisions of the Internal Revenue Code of 1986, as amended (the "Code"). Under the Code, a life insurance company's taxable income incorporates all income, including life and health premiums, investment income, and certain decreases in reserves. The Code currently establishes a maximum corporate tax rate of 35% and imposes a corporate alternative minimum tax rate of 20%. See Item 7 and Note 7 of the Notes to Consolidated Financial Statements.

The Code currently requires capitalization and amortization over a five to ten year period of certain policy acquisition costs incurred in connection with the sale of certain insurance products. Prior tax laws permitted these costs to be deducted as incurred. These provisions apply to life, health, and annuity business. Certain proposals to make additional changes in the federal income tax laws, including increasing marginal tax rates, and regulations affecting insurance companies or insurance products, continue to be considered at various times in the United States Congress and by the Internal Revenue Service. The Company currently cannot predict whether any additional changes will be adopted in the foreseeable future or, if adopted, whether such measures will have a material effect on its operations.

Reserves. In accordance with applicable insurance laws, the Life Insurance Subsidiaries have established and carry as liabilities actuarially determined reserves to meet their policy obligations. Life insurance reserves, when added to interest thereon at certain assumed rates and premiums to be received on outstanding policies, are required to be sufficient to meet policy obligations. The actuarial factors used in determining reserves in the statutory basis financial statements are based upon statutorily-prescribed mortality and interest rates. Reserves maintained for health insurance include the unearned premiums under each policy, reserves for claims that have been reported but not yet paid, and reserves for claims that have been incurred but have not been reported. Furthermore, for all health policies under which renewability is guaranteed, additional reserves are maintained in recognition of the actuarially-calculated probability that the frequency and amount of claims will increase as policies persist. The Life Insurance Subsidiaries do not continue accumulating reserves on reinsured business after it is ceded. The Life Insurance Subsidiaries are required to maintain reserves on reinsured business assumed on a basis essentially comparable to direct insurance reserves. Reinsurance business assumed is presently insignificant in amount.

The reserves carried in the financial statements included in this Form 10-K are calculated on the basis of accounting principles generally accepted in the United States and differ from the reserves specified by laws of the various states, which govern preparation of financial statements on the statutory basis of accounting for the Life Insurance Subsidiaries. These differences arise from the use of different mortality and morbidity tables and interest assumptions, the introduction of lapse assumptions into the reserve calculation, and the use of the level premium reserve method on all insurance business. See Note 1 of the

Notes to Consolidated Financial Statements, for certain additional information regarding reserve assumptions under accounting principles generally accepted in the United States.

Employees. As of March 25, 2003, 72 people, excluding agents, were employed by the Company. As of that date, the Company had approximately 3,500 independent agents licensed to sell its products.

ITEM 2. PROPERTIES

The Company owns, through Citizens Security, a three-story, 63,000 square foot

office building in suburban Louisville, Kentucky completed in 1988. The Company and its Subsidiaries occupy about 31% of the building for their headquarters and home offices. The Company leases the remaining space to tenants under leases of various duration. Market conditions for this property are generally favorable and, in management's opinion, the property is adequately covered by insurance. Currently, the Company's policy is not to invest in additional real estate or real estate mortgages, although a change in such policy would not require a vote of security holders. In addition, the Company's current bank lending agreement precludes investment in additional real estate and in mortgages with a loan-to-appraised-value ratio of more than 75%.

ITEM 3. LEGAL PROCEEDINGS

An action was filed against United Liberty in the Court of Common Pleas for Butler County, Ohio by two policyholders in June 2000. The Complaint refers to a particular class of life insurance policies that United Liberty issued over a period of years ending around 1971. It alleges that United Liberty's dividend payments on these policies from 1993 through 1999 were less than the required amount. It does not specify the amount of the alleged underpayment but implies a maximum of about $850,000. The plaintiffs also allege that United Liberty is liable to pay punitive damages, also in an unspecified amount, for breach of an implied covenant of good faith and fair dealing to the plaintiffs in relation to the dividends. The action has been certified as a class action on behalf of all policyholders who were Ohio residents and whose policies were still in force in 1993. United Liberty has denied the material allegations of the Complaint and is defending the action vigorously. Pre-trial discovery is continuing. United Liberty has filed a motion for summary judgment to which the plaintiffs have not yet responded. At United Liberty's request, an initial mediation session has been completed and negotiations are continuing. As a pre-requisite for the mediation, United Liberty offered to settle the matter for payments over time, which would include attorneys' fees, and which would be contingent upon an exchange or reformation of the insurance policies currently owned by the members of the class. At this stage of the litigation, the Company is unable to determine whether an unfavorable outcome of the action is likely to occur or, alternatively, whether the chance of such an outcome is remote. Therefore, at this time, management has no basis for estimating potential losses, if any. There are no other material legal proceedings pending against the Company or its subsidiaries or of which any of their property is the subject other than routine litigation incidental to the business of the Company and its subsidiaries. There are no material proceedings in which any director, officer, affiliate or shareholder of the Company, or any of their associates, is a party adverse to the Company or any of its subsidiaries or has a material interest adverse to the Company or any of its subsidiaries.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matter was submitted during the fourth quarter of the fiscal year covered by this Form 10-K to a vote of the Company's security holders, through the solicitation of proxies or otherwise.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

As of March 25, 2003, there were approximately 2,500 holders of record of the

Company's Class A Stock, its only class of common equity. The Class A Stock is currently eligible for quotation on the National Association of Securities Dealers, Inc.'s Small-Cap Market ("NASDAQ") under the trading symbol CNFL. Trading volume in 2002 was about 10% of the average shares outstanding during the year and trading volume by non-affiliates was about 25% of the average shares owned by non-affiliates during the year.

The following table summarizes quarterly high and low bid quotations for the Class A Stock in 2002 and 2001 as reported by NASDAQ. Such quotations reflect inter-dealer prices and do not include retail markup, markdown, or commission, and may not necessarily represent actual transactions.

	Bid Quotations for Class A Stock	
Quarter Ended	High Bid	Low Bid
December 31, 2002	$ 5.260	$ 3.350
September 30, 2002	$ 8.000	$ 3.800
June 30, 2002	$ 8.900	$ 7.500
March 31, 2002	$ 9.000	$ 8.050
December 31, 2001	$ 9.750	$ 8.100
September 30, 2001	$ 10.000	$ 8.600
June 30, 2001	$ 10.875	$ 9.350
March 31, 2001	$ 11.500	$ 10.375

The Company has not paid a dividend on the Class A Stock. The Board of Directors of the Company has not adopted a dividend payment policy; however, dividends must necessarily depend upon the Company's earnings and financial condition, applicable legal restrictions, and other factors relevant at the time the Board of Directors considers a dividend policy. The Company is subject to a loan agreement covenant that prevents it from paying dividends on the Class A Stock without the consent of the lender except to the extent it can meet certain requirements relating to the ratio of its outstanding borrowings compared to dividends and income before interest expense, amortization, depreciation and income tax expense for (5) consecutive quarters and provided that there is no default or potential default under the loan agreement. As of January 2003, the bank loan covenant precludes the Company from paying any dividends. Cash available for dividends to shareholders of the Company must initially come from income and capital gains earned on its investment portfolio, management service fees and dividends paid by the Insurance Subsidiaries, and Citizens Security's repurchase of its preferred stock owned by the Company. Provisions of the Kentucky Insurance Code subject transactions between the Insurance Subsidiaries and their respective parents, including dividend payments, to certain standards generally intended to prevent such transactions from adversely affecting the adequacy of the Insurance Subsidiaries' capital and surplus available to support policyholder obligations. See Item 1. "Description of Business -- State Insurance Regulation." In addition, under the Kentucky Business Corporation Act, the Company may not pay dividends if, after giving effect to a dividend, it would not be able to pay its debts as they become due in the usual course of business or if its total liabilities would exceed its total assets.

Below is summary of securities available for issuance under equity compensation plans.

	a	b	c
Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securitie Available for Future Equity Compensation Pl Securities Reflected

Equity compensation plans approved by security holders	0	Not applicable	110,000
Equity compensation plans not approved by security holders	0	Not applicable	0
Total	0	Not applicable	110,000

ITEM 6. SELECTED FINANCIAL DATA

Year Ended December 31	2002	2001	2000	
RESULTS OF OPERATIONS				
Premiums and other considerations	$38,479,150	$28,744,376	$23,822,424	$20,8
Investment and other income, net	6,093,036	6,530,372	6,291,309	6,0
Policy benefits and reserve change	31,878,748	22,989,732	19,400,397	17,0
Commissions, expense, amortization, net	13,247,015	11,824,589	10,676,953	10,0
Segment profit (loss)	(553,577)	460,427	36,383	(1
Realized investment gains (losses), net	(2,469,768)	(7,911,829)	1,180,879	9,3
Interest expense	305,715	532,962	769,132	5
Cumulative effect - accounting change	---	(311,211)	---	
Income tax expense (benefit)	(757,000)	(2,090,000)	210,000	2,2
NET INCOME (LOSS)	$(2,572,060)	$(6,205,575)	$ 238,130	$ 6,4
NET INCOME (LOSS) APPLICABLE TO COMMON STOCK	$(2,572,060)	$(6,205,575)	$ 238,130	$ 6,4
NET INCOME (LOSS) PER SHARE:				
Before accounting change	$(1.50)	$(3.39)	$0.14	
Basic	$(1.50)	$(3.57)	$0.14	
Diluted	$(1.50)	$(3.57)	$0.14	
FINANCIAL POSITION				
Total assets	$ 148,441,532	$136,597,083	$135,538,006	$137,9
Notes payable	$ 7,779,168	$ 7,095,834	$ 8,000,000	$ 8,5
Shareholders' equity	$ 17,757,632	$ 20,002,483	$ 23,274,109	$ 28,0
Shareholders' equity per share	$10.53	$11.65	$13.24	
INVESTMENTS				
Average cash and invested assets	$117,460,459	$112,982,243	$121,807,002	$115,0

Average equity portfolio (cost basis)	$6,966,585	$ 9,736,625	$ 20,017,915	$ 20,6
Investment income yield	4.8%	5.6%	4.9%	
Change in unrealized investment gains (losses), net of tax	$ 466,654	$ 3,019,188	$ (4,896,265)	$ 2

LIFE INSURANCE DATA				
Premiums	$ 28,948,728	$ 19,362,994	$ 14,553,493	$ 12,4
Insurance in force, net at end of period	$696,520,000	$703,288,000	$706,044,000	$646,4

HEALTH INSURANCE DATA				
Premiums	$ 9,530,422	$ 9,381,382	$ 9,268,931	$ 8,4
Benefit ratio	69.5%	67.9%	66.7%	

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Company's 2002 net loss was $2,572,000 compared a net loss of $6,206,000 in 2001 and net income of $238,000 in 2000. Comprehensive losses (which combine net losses and net unrealized gains and losses) were $2,105,000, $2,875,000, and $4,658,000 for 2002, 2001, and 2000, respectively. During 2002, the Company continued to be adversely affected by declining equity markets along with declining interest yields on its fixed income investment portfolio. The majority of the 2001 and 2000 declines in net income and the comprehensive losses were attributable to adverse securities markets during those years, including the effects of declines in the telecommunications and technology sectors, a general economic recession and terrorist events.

During 2002, the Company achieved a 34% or $9,735,000 increase in premiums. A 114% increase in the Preneed Life segment accounts for essentially all of the net increase, along with approximate 2.5% increases in the Home Service Life and Dental segments, partially offset by moderate reductions in Broker Life and Other Accident and Health. Pretax segment profit (loss), excluding realized investment gains and losses and interest expense, was ($554,000), $460,000 and $36,000 for 2002, 2001, and 2000 respectively. The decline in 2002 was primarily attributable to lower interest yields and adverse mortality, while the 2001 improvement was primarily attributable to increased Preneed Life production.

The Company repurchased 29,987, 41,400 and 9,000 shares of its common stock during 2002, 2001, and 2000 respectively, at average prices of $4.65, $9.58 and $11.58 per share, respectively.

The Company manages its operations in five business segments, Home Service Life, Broker Life, Preneed Life, Dental, and Other Health. Products in all five segments are sold through independent agency operations. Home Service Life consists primarily of traditional life insurance coverage sold in amounts of $10,000 and under to middle and lower income individuals. This distribution channel is characterized by a significant amount of agent contact with customers throughout the year. Broker Life product sales consist primarily of simplified issue and graded-benefit policies in amounts of $10,000 and under. Other products in the Broker Life segment which comprise a significant portion of existing business include group life, universal life, annuities and participating life coverages. Preneed Life products are sold to individuals in connection with prearrangement of their funeral and include single and multi-pay

coverages, generally in amounts of $10,000 and less. These policies are generally sold to older individuals at increased premium rates. Dental products are term coverages generally sold to small and intermediate size employer groups. Other Health products include various accident and health coverages sold to individuals and employer groups. Profit or loss for each segment is reported on a pretax basis, without an allocation of realized investment gains or interest expense.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's discussion and analysis of its financial condition and results of operations are based on its consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. Preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates, including those related to investments, agent receivables, intangible assets, policy liabilities, income taxes, regulatory requirements, contingencies and litigation. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The Company believes the following accounting policies, judgments and estimates, which have been discussed with the Audit Committee of the Board of Directors, critically impact preparation of its consolidated financial statements.

Investment in Debt and Equity Securities. The Company holds debt and equity interests in a variety of companies, many of which are seeking to exploit recent technology advancements. The majority of these are publicly traded and many have experienced volatile market prices. We periodically evaluate whether the declines in fair value of our investments are other-than-temporary. These evaluations involve significant judgment. Our evaluation consists of a review of qualitative and quantitative factors, including analysis of the company's competitive position in its markets, deterioration in the financial condition of

the issuer, downgrades of the security by a rating agency, and other publicly available issuer-specific news or general market conditions. Declines in fair values of securities deemed to be other-than-temporary are included in net income as realized investment losses. Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the current carrying value of the investments, thereby possibly requiring an impairment charge in the future.

Goodwill and Intangible Impairment. Assessing recoverability of the Company's goodwill and other intangibles (including deferred policy acquisition costs and value of insurance acquired) requires assumptions regarding estimated future cash flows and other factors (see Policy Liabilities below) to determine the fair value of the respective assets. If these estimates or their related assumptions change in the future, the Company may be required to record impairment charges for these assets not previously recorded. On January 1, 2002 the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," and performed an evaluation for potential impairment. The Company concluded that no impairment adjustment was necessary for its goodwill or other intangible assets.

Policy Liabilities and Policy Intangible Assets. Establishing policy liabilities

and related intangible assets, including deferred acquisition costs and the value of acquired insurance, for the Company's long-duration insurance contracts requires making many assumptions, including policyholder persistency, mortality rates, investment yields, discretionary benefit increases, new business pricing, and operating expense levels. The Company evaluates historical experience for these factors when assessing the need for changing current assumptions. However, since many of these factors are interdependent and subject to short-term volatility during the long-duration contract period, substantial estimates and judgment are required. Accordingly, if actual experience emerges differently from that assumed, material financial statement adjustments could be required.

Deferred Taxes. The Company records a valuation allowance to reduce its deferred tax assets to the amount that it believes is more likely than not to be realized. In assessing the need for the valuation allowance, the Company has considered ongoing prudent and feasible tax planning strategies but has not assumed future taxable income. In the event the Company were to determine that it would be able to realize its deferred tax assets in the future in excess of its net recorded amount, an adjustment to deferred tax assets would increase income in the period such determination was made. Likewise, should the Company determine that it would not be able to realize all or part of its net deferred tax assets in the future, an adjustment to deferred tax assets would be charged to income in the period such determination was made.

Litigation. As further described in Note 12 of the Notes to Consolidated Financial Statements, United Liberty is party to an outstanding lawsuit concerning payment of policyholder dividends. The Company is currently unable to determine whether an unfavorable outcome of this action is likely, and no provision has been recorded for an unfavorable outcome. Accordingly, if an unfavorable outcome occurs, a financial statement adjustment would be required.

ACQUISITIONS

National Affiliated Investors Life

On July 7, 2000, the Company acquired, through an assumption reinsurance agreement, 100% of the inforce business of National Affiliated Investors Life Insurance Company ("NAIL") for a net cash purchase price of approximately $355,000 (the "NAIL Acquisition"). The acquisition was coordinated through the National Organization of Life and Health Guaranty Associations. The acquired business consists primarily of individual life insurance business with policy reserves and annual premium of approximately $3,500,000 and $300,000, respectively.

Citizens Insurance Company

On October 14, 1999, the Company acquired 100% of the stock of Citizens Insurance (formerly Kentucky Insurance Company) from an unaffiliated insurance holding company (the "Citizens Insurance Acquisition"). Citizens Insurance is licensed as a property and casualty insurance company in six states and has approximately $3.6 million of statutory capital and surplus; however, it currently has no insurance operations. The aggregate purchase price for the

Citizens Insurance Acquisition was approximately $3,550,000 (including net costs associated with the transaction of approximately $50,000).

United Liberty Life Insurance Company

On May 12, 1998, the Company and Citizens Security acquired 100% of the common stock of United Liberty from an unaffiliated insurance holding company (the

"United Acquisition"). The aggregate purchase price for the United Acquisition was approximately $7,076,000 (including net costs associated with the acquisition of approximately $445,000). In conjunction with the acquisition, the seller retained approximately $2,100,000 of United Liberty's real estate related and other assets, which were replaced with cash by Citizens Security.

FINANCIAL POSITION

Assets. At December 31, 2002, the Company's available-for-sale fixed maturities had a fair value of $103,953,815 and amortized cost of $101,161,174. The Company's fixed maturities portfolio increased approximately 33% during 2002 and 5% during 2001, on an amortized cost basis. These increases are primarily attributable to Preneed Life sales growth. Shown below is a distribution by rating category of the Company's fixed maturities portfolio as of December 31, 2002.

Standard & Poor's Corporation Rating	Amortized Cost 1	Fair Value 2
Investment grade:		
AAA to A-	$ 80,102,193	$ 83,103,323
BBB+ to BBB-	15,852,485	16,054,042
Total investment grade	95,954,678	99,157,365
Non-investment grade:		
BB+ to BB-	2,651,515	2,589,976
B+ to B-	1,431,094	1,282,473
CCC+ to C	658,941	461,650
CI to not rated	464,946	462,351
Total non-investment grade	5,206,496	4,796,450
Total fixed maturities	$101,161,174	$103,953,815

1 Net of write-downs on bonds whose decline in value is believed to be other-than-temporary
2 Fair values as of December 31, 2002 were obtained primarily from Interactive Data Corporation.

The Company believes it has a well diversified portfolio and has no plans to adjust its non-investment grade portfolio significantly, unless necessary to satisfy requirements of state regulators or rating agencies. The Company purchases non-investment grade bonds to obtain higher yields or convertible features and attempts to reduce credit risk by portfolio diversification. Non-investment grade securities comprised 5.1% and 6.7% of the fixed maturities portfolio, on an amortized cost basis at December 31, 2002 and 2001, respectively. During 2002, the Company recognized approximately $501,000 of impairment losses on fixed maturities, with the majority of these related to the airline and telecommunication industries. The Company is monitoring its fixed maturity portfolio and, although it has no specific projections, if the overall economy does not improve, additional impairments could occur during 2003.

Shown below are the Company's four largest holdings in non-investment grade bonds by a single issuer as of December 31, 2002.

	Non-Investment Grade	
December 31, 2002	Amortized Cost	Fair Value

Largest	$507,176	$525,000
Second largest	449,643	267,486
Third largest	408,411	390,000
Fourth largest	387,727	385,084
Total	$1,752,957	$1,567,570

The Company had no guarantee or other type of enhancement associated with the issuers represented above.

During 2002, the Company's investment in equity securities increased $53,000 on a cost basis and decreased $355,000 on a fair value basis, after decreasing $6,622,000 and $4,461,000 on a cost and fair value basis, respectively, during 2001. As of December 31, 2002 and 2001, there were $653,000 and $1,062,000 respectively, of unrealized gains on equity securities, compared to $1,099,000 of unrealized losses at December 31, 2000.

The Company reviews its marketable investments each quarter to determine if there have been declines in their value that in management's opinion are other-than-temporary. These reviews can involve qualitative and quantitative information relating to an individual company or industry and general factors impacting the economy. However, due to wide market fluctuations occurring during the past two years, determining whether declines are temporary has become much more complex and judgmental. These reviews resulted in the recognition of impairment losses on equity securities totaling $754,000 during 2002 ($141,000, $315,000, $250,000 and $48,000 for the first through fourth quarters, respectively). In addition, $501,000 of impairment losses were recognized on fixed maturities during 2002 ($133,000, $88,000, and $280,000 during the second, third, and fourth quarters, respectively). During 2002, equity securities were sold which contained impairment writedowns of $1,531,000.

Citizens Security owns the building in which the Company and its subsidiaries maintain their home offices. They occupy approximately 31% of the building with the balance leased to third-party tenants. Market conditions for this property are generally favorable. An updated appraisal obtained during 2002 indicates the market value of the property is approximately $2,500,000 higher than its carrying value.

At December 31, 2002 the Company has recorded $756,000 of goodwill and $13,533,000 of other intangible assets for deferred policy acquisition costs and value of insurance acquired. As noted in the above discussion of critical accounting policies and estimates, these intangibles, and the recorded value of policy liabilities, are based on many assumptions that require substantial estimates and judgment. In connection with adoption of SFAS No. 142, the Company reassessed the assumptions supporting these values. Although no impairment was considered necessary, a continued historically low interest rate environment could require adjustment of these recorded values.

Liabilities. A comparison of total policy liabilities as of December 31, 2002, 2001 and 2000 is shown below. Approximately 87% of the 2002 total consists of insurance policy benefit reserves while policyholder deposit liabilities represent 13% of the total.

Year Ended December 31	2002	2001	2000
Home Service Life	$ 33,970,723	$ 32,609,959	$ 31,543,557
Broker Life	45,054,589	44,414,974	44,631,499
Preneed Life	38,971,203	27,512,646	23,094,830
Dental	524,249	565,119	610,111
Other Health	2,194,869	2,137,079	2,143,247

Total	$120,715,633	$107,239,777	$102,023,244

Home Service Life sales have been favorable in recent years, with net growth in policy liabilities of 4.2% and 3.4% in 2002 and 2001, respectively, through a combination of attracting new producers and continuing to focus on meeting the needs of existing customers and agents. The Broker Life segment's 2002 policy liability net increase of $640,000 resulted primarily from normal aging of existing reserves. A significant portion of the $217,000 decrease in Broker Life policy liabilities during 2001 relates to expiration of a withdrawal waiting period for the NAIL business acquired during 2000. During 2002 and 2001, the Company increased Preneed Life production through arrangements with several third party marketing groups and its internal marketing organization, with significant growth occurring in Ohio, Pennsylvania, Kentucky, Indiana, and North Carolina. A significant portion of this growth consists of single premium policies whereby individuals are fully funding their funeral costs. Due to the lower interest rate environment, the Company has reduced the rate of annual increases in benefit amounts and is in the process of reducing some agent commission schedules. Accordingly, depending on competitor responses, future business growth could be adversely impacted. The Company's Dental products are annual term coverages; accordingly, policy liabilities for this segment are not significant. The Other Health segment business is not a significant marketing focus.

Shown below is a progression of the Company's policyholder deposit activity for the year ended December 31, 2002.

Year Ended December 31, 2002	Total	Annuity and Other	Universal Life
Beginning Balance	$15,917,731	$ 9,907,941	$ 6,009,790
Deposits	741,863	168,084	573,779
Withdrawals	(1,698,063)	(781,182)	(916,881)
Interest Credited	781,762	510,239	271,523
Ending Balance	$15,743,293	$ 9,805,082	$ 5,938,211

As indicated above, total policyholder deposits decreased by a net $174,000 during 2002. The Company is not devoting significant marketing effort towards Annuity, Universal Life and other deposit products and has elected not to aggressively compete in crediting excess interest on such products.

CONSOLIDATED RESULTS AND ANALYSIS

Premiums and Other Considerations. The following table details premiums and other considerations received during the past three fiscal years.

Year Ended December 31	2002	2001	2000
Home Service Life	$7,334,030	$7,152,242	$6,906,473
Broker Life	3,621,053	3,812,841	3,664,072
Preneed Life	17,993,645	8,397,911	3,982,948
Dental	8,182,483	7,988,620	7,892,356
Other Health	1,347,939	1,392,762	1,376,575
Total	$ 38,479,150	$ 28,744,376	$ 23,822,424

Home Service Life premium increased 2.5% and 3.6% during 2002 and 2001,

respectively. New sales levels continue to be favorable, at levels which more than exceed normal policy lapses. The Company continues to attract a number of successful, experienced Home Service agents without subsidizing inexperienced agents. In addition, the Company's program to automate and streamline agent field accounting continues to expand with favorable reaction among the agency force. During early 2003 the Company terminated a small Home Service marketing joint venture in two southern states with a much larger property and casualty insurance carrier. To mitigate effects of the lower interest rate environment, during the second quarter of 2003 the Company will be introducing premium rate increases on its Home Service products.

The 5% decrease in Broker Life premium during 2002 resulted from reduction of business provided by certain larger brokers during 2002 and continuing pressure from the overall economic slowdown on middle and lower-income consumers. The

Company is evaluating opportunities for revising its product design and commission rates to counteract the softening in demand for its simplified issue and graded benefit life policies. The 4.1% Broker Life premium increase during 2001 is primarily attributable to receiving a full year of premium on the NAIL business compared to receiving six months of additional premium during 2000.

The 114% increase in Preneed Life premium during 2002 and the 111% increase during 2001 resulted from intensified marketing efforts aimed at defining the Company as a committed participant in this market, successfully negotiating competitive third-party marketing agreements, implementing various product enhancements, and positive referrals from customers who comment favorably on the Company's organization and customer service. However, as described above, in early 2003, the Company modified certain policy benefits and commissions which may reduce future premium production.

The 2.4% growth in Dental premium during 2002 resulted primarily from normal inflationary increases, while the 1.2% growth during 2001 was impacted by loss of a large group case. During the past two years, new business production has become increasingly competitive as larger providers expand their marketing initiatives. However, the Company has historically maintained strong customer and agent loyalty by continuing to improve customer service, including sales and administrative support functions.

The Company has not been actively marketing Other Health coverages for several years. However, in response to agent requests, certain cancer and disability protection products have been updated and promoted. Pricing, underwriting, and claims experience on these products are closely monitored.

Investments. The Company monitors its available-for-sale fixed maturities and equity securities to assure they are strategically positioned within the current market environment. This practice has historically resulted in holding significant equity security positions, which tend to dampen current income yields in favor of an overall total return focus. The Company's equity securities comprised 6.5% and 8.6% of its total investment portfolios at December 31, 2002 and 2001, respectively. The Company's investment income yields were 4.8%, 5.6%, and 4.9% for 2002, 2001, and 2000, respectively. The 2002 yield decline resulted primarily from substantially lower interest rates on new investments and the Company's 33% net addition to its fixed maturity portfolio during the year, much of which is attributable to additional Preneed Life business. The 2001 yield increase resulted primarily from carrying significantly lower levels of equity securities and higher levels of fixed maturity investments. Although the Company's total return on investments has historically been very favorable, returns for the past three years have been severely impacted by declines in the telecommunications and technology sectors, a general economic recession and the effect of terrorist events on the securities markets.

As detailed below, net realized and unrealized investment losses totaled approximately $(11,953,000) for the three years ended December 31, 2002, while net realized and unrealized gains totaled approximately $14,200,000 for the two years ended December 31, 1999. The Company does not anticipate continued severe deterioration in the securities markets, although some additional losses on fixed income securities may occur if the overall economic slowdown continues. At December 31, 2002, the Company's investment portfolios are somewhat more conservatively positioned compared to prior years, and they contain a net unrealized gain outstanding of $3,446,000. Below is an approximate calculation of investment income yields and total return rates for the five years ending December 31, 2002.

Year Ended December 31,	2002	2001	2000	1999
Investment Income	$5,665,596	$6,274,143	$5,993,362	$5,885,312
Gains and Losses:				
Fixed Maturities:				
Realized gains (losses)	(228,710)	(1,260,092)	1,061,089	243,949
Unrealized gains (losses)	1,130,402	2,303,205	(1,655,112)	(1,804,929)
Net Fixed Maturities	901,692	1,043,113	(594,023)	(1,560,980)
Equity Securities:				
Realized gains (losses)	(2,241,058)	(7,123,269)	119,790	9,131,390
Unrealized gains (losses)	(408,399)	2,160,985	(5,812,184)	2,238,293
Net Equity Securities	(2,649,457)	(4,962,284)	(5,692,394)	11,369,683
Total Gains and Losses	(1,747,765)	(3,919,171)	(6,286,417)	9,808,703
Total Return	$3,917,831	$2,354,972	$(293,055)	$ 15,694,015
Average Cash and Investments	$117,460,000	$112,980,000	$121,810,000	$115,050,000
Yield - Income	4.8%	5.6%	4.9 %	5.1%
Yield - Total Return	3.3%	2.1%	(0.2)%	13.6%

Segment Earnings. The 2002 loss before income tax and the cumulative effect of a change in accounting principle was $3,329,000 compared to a loss of $7,984,000 in 2001 and income of $448,000 in 2000. Pretax profit (loss) is shown below for the Company's five business segments, along with total realized investment gains and interest expense.

Year Ended December 31	2002	2001	
Segment Profit (Loss):			
Home Service Life	$ 275,809	$ 382,723	$
Broker Life	(265,488)	74,960	
Preneed Life	(670,349)	(264,488)	

Dental	297,740	256,385	
Other Health	(191,289)	10,847	
Segment Totals	(553,577)	460,427	
Net realized investment gains (losses)	(2,469,768)	(7,911,829)	1
Interest expense	305,715	532,962	
Income (Loss) before income tax and cumulative effect of a change in accounting principle	$ (3,329,060)	$ (7,984,364)	$

During 2002, the Company's investment income yield declined approximately 73 basis points. Accordingly, since the Company allocates investment income to each business segment based on average net policy reserves, each of the three life insurance segments were adversely impacted by investment yields during 2002. In addition, the 2002 Home Service Life profit was adversely impacted by increased mortality, partially offset by lower expenses, while 2001 profit benefited from sales growth and improved mortality results. The 2002 Broker Life earnings decrease resulted primarily from the lower investment yield while the 2001 decrease resulted primarily from increased mortality and expenses. The 2002 Preneed Life loss resulted from lower investment yields, unfavorable mortality,

and increased expenses. During 2002, the Company accepted a significant amount of single-premium business, which generally has higher than average mortality rates. In addition, significant management and marketing resources were devoted to this business. To improve profitability, annual benefit growth rates were reduced twice during 2002, and in early 2003, certain commission rates were reduced and agent contracts revised to encourage production of the more profitable multi-pay products. The 2001 Preneed Life loss improved approximately $563,000 from the prior year while premium increased approximately 111%. This volume growth leveraged fixed costs and improved per-policy profitability. Although the Company is optimistic about improving profitability in this highly competitive market, if adverse profitability trends continue, several options are available. These options, including further lowering discretionary annual benefit increases and adjusting premiums and commissions on new business, could further adversely impact the Company's ability to compete for new business.

Information regarding Dental profitability is included below. The "contribution margin" shown below is a direct margin without allocable investment income and general expense.

Year Ended December 31	2002	2001	2000
Premium	$8,182,483	$7,988,620	$7,892,356
Claims and Reserves	$5,634,940	$5,551,624	$5,369,742
Contribution Margin	$1,560,208	$1,465,017	$1,516,948
Claim Ratio	68.9%	69.5%	68.0%

The overall Dental contribution margin increased slightly during 2002 due to improved claim levels. The 2001 contribution margin decrease resulted from somewhat higher claims. Also, beginning in 2001 the Company began encountering more competition as additional insurers are expanding in the Dental market and Dental providers are continuing to provide higher levels of care to patients. The Company is continuing its ongoing efforts to maintain profitability in this line by reconfiguring products to provide adequate margins for the various dental procedures, utilizing a third-party company to provide expert assistance with ongoing adjudication of claims, and continuing its program of aggressive renewal underwriting and re-rating. The Company has not devoted significant

marketing effort towards its Other Health products in recent years. However, during 2002, a significant increase in disability claims occurred, with a concentration in New Jersey. The Company has strengthened underwriting practices in this area and has taken steps towards filing for a rate increase on its disability products. In addition, during 2001 the Company implemented significant rate increases on certain older blocks of Other Health business.

Income Taxes. Historically, the Company has experienced a relatively low effective income tax rate, due primarily to the small life insurance company deduction. The effective rate was approximately 23% and 26% in 2002 and 2001, respectively. The effective rate was much higher in 2000, due to state and local income taxes on the parent company's investment gains along with an increased valuation allowance on deferred tax assets.

The small life insurance company deduction allows the Life Insurance Subsidiaries to reduce their taxable income by 60% before computing their current provisions for regular or alternative minimum tax. However, for purposes of computing deferred income tax liabilities under the provisions of Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes", the Company is precluded from assuming the small life insurance company deduction will be available in the future. Accordingly, by disallowing this deduction, SFAS No. 109 significantly increases the deferred taxes on the Life Insurance Subsidiaries' temporary differences. Thus, when a significant increase or decrease occurs in the Company's net temporary differences, the related deferred tax is computed using the 34% federal tax rate, whereas tax may actually be paid on these net liabilities (when realized) at a rate potentially as low as 17% (the alternative minimum tax rate after application of the allowable small life insurance company deduction). The Company's gross deferred federal income tax liabilities and assets are more fully discussed in Note 7 of the Notes to Consolidated Financial Statements. All deferred tax assets of the Company are realizable by offset against existing deferred tax liabilities or by carryback to recapture prior years' taxes paid on operating income and capital gains. The deferred tax assets are offset, to some extent, by valuation allowances related to the Company and to the Life Insurance Subsidiaries. Due to the impact of the small life insurance company deduction, the Life Insurance Subsidiaries record a valuation allowance to reduce deferred tax assets (associated with temporary differences) to their expected benefit rate of approximately 17%, rather than 34%. The Company's valuation allowance is designed to reduce deferred tax assets to their estimated ultimate realization value.

Statutory Insurance Information. For insurance regulatory and rating purposes, the Insurance Subsidiaries report on the basis of statutory accounting principles ("SAP"). As described in Note 8 of the Notes to Consolidated Financial Statements, effective January 1, 2001 portions of SAP were revised by a process called "Codification". In recent years, various state insurance departments and the NAIC have expressed concern, essentially about the "rate of return" earned by holders of small face amount life policies, potentially including Preneed policies. Although the Company does not believe calculating a simple "rate of return" or premium "pay-back" measure is meaningful for traditional life insurance products, certain state insurance regulators are considering actions that could alter the profitability of existing contracts or eliminate small face amount policies as a viable product offering. During 2002, A.M. Best Company ("Best") affirmed Citizens Security's B- rating. This rating was previously lowered from a B in 2001. United Liberty's rating has remained at B- by Best since it was acquired in 1998, and Citizens Insurance, due to its lack of insurance operations, is not rated.

During December 2002, Citizens Financial strengthened the statutory capital position of Citizens Security by acquiring $2,000,000 of Citizens Security

redeemable preferred stock. During January 2001, Citizens Financial contributed 100% of the capital stock of Citizens Insurance to Citizens Security. The statutory value of this contribution was $3,540,555. Citizens Security has reported its investments in United Liberty and Citizens Insurance on the equity method of accounting, since their acquisition in 1998 and 2001, respectively. However, beginning in 2001, Codification changed the statutory equity method of accounting to preclude a parent insurer from recording as income, its share of undistributed subsidiary earnings. Accordingly, Citizens Security's net income includes United Liberty's net earnings of $404,553, $234,853, and $289,489, in 1998, 1999, and 2000, respectively. For 2001 and 2002, Citizens Security reported as income the $292,000 and $214,000 respectively, of dividend distributions which it received from United Liberty. At December 31, 2002, Citizens Security reported its investments in United Liberty and Citizens Insurance at their statutory equity values of $2,159,092 and $3,783,528, respectively. To provide a more detailed understanding of Citizens Security's operations, shown below are SAP basis net income, net operating income, statutory capital and surplus, asset reserves, and capital ratios for Citizens Security for the five years ended December 31, 2002.

Year Ended December 31	Net Income (Loss)	Net Operating Income (Loss)	Statutory Capital and Surplus	Asset Valuation Reserves1	Capital Ratio2
2002	$(1,184,496)	$ (64,815)	$9,903,639	$ 862,732	11.6%
2001	$(3,497,701)	$ 361,863	$9,687,289	$ 978,418	13.6%
2000	$1,868,575	$ 715,250	$8,315,902	$1,589,735	13.7%
1999	$4,945,708	$ 568,436	$12,942,331	$4,335,111	22.4%
1998	$3,662,188	$1,105,631	$11,227,528	$3,606,655	20.5%

1 Asset Valuation Reserves are statutory liabilities that act as contingency reserves in the event of extraordinary losses on invested assets and as a buffer for policyholders' surplus to reduce the impact of realized and unrealized investment losses. The 1998 through 2002 amounts also include United Liberty's asset valuation reserves.

2 Represents Statutory Capital and Surplus plus Asset Valuation Reserves divided by invested assets plus cash.

During 2002, statutory capital and surplus and asset valuation reserves increased approximately $101,000. This increase resulted primarily from the $2,000,000 issuance of preferred stock described above, net of the $1,184,000 net loss for the year and $950,000 of unrealized losses. During 2001, statutory capital and surplus and asset valuation reserves increased approximately $760,000. This increase resulted primarily from the Citizens Insurance capital contribution noted above, plus $1,082,000 of unrealized gains offsetting the $3,498,000 net loss and a $572,000 increase in nonadmitted assets. During 2000, statutory capital and surplus and asset reserves decreased by approximately $7,413,000. This decrease resulted primarily from $1,869,000 of statutory net income offset by $7,875,000 of unrealized losses and a $1,200,000 redemption of Citizens Security's preferred capital stock. During 1999, statutory capital and surplus and asset reserves increased by approximately $2,443,000. This increase resulted primarily from $4,946,000 of statutory net income offset by a $1,200,000 redemption of preferred capital stock, and a $1,000,000 shareholder dividend paid. During 1998, statutory capital and surplus and asset reserves increased by approximately $2,454,000. This increase resulted primarily from $3,662,000 of statutory net income offset by a $1,500,000 redemption of preferred capital stock, along with unrealized investment gains.

In addition to the statutory totals shown above, Citizens Insurance generated statutory net income of approximately $63,000, $76,000, and $93,000 during, 2002, 2001, and 2000, respectively without remitting any dividends to its parent.

Statutory capital and surplus, specifically the component called surplus, is used to fund the expansion of an insurance company's first year individual life and accident and health sales. The first year commission and underwriting expenses on such sales will normally consume a very high percentage of, if not exceed, first year premiums. Accordingly, a statutory loss (surplus strain) often occurs on these sales during the first policy year. Historically, the Company's level of life insurance sales has not significantly impacted statutory surplus. However, as multi-pay Preneed Life sales increase, the Company anticipates that surplus strain will dampen statutory earnings.

CASH FLOW AND LIQUIDITY

Due to losses during the past three years and the adverse impact of the low interest rate environment on operating results, during 2002 the Company borrowed $2,000,000 from its Chairman to strengthen the statutory capital position of its principal insurance subsidiary. The Company also has $5,779,168 of commercial bank debt outstanding, with scheduled repayments due through 2007. During 2002, the Company did not comply with a loan covenant (debt to earnings ratio) on this debt and received a waiver of such violation through December 31, 2002. However, since the Company is not assured of meeting this covenant throughout 2003, the full balance of $5,779,168 can be considered payable within one year. Although the Company does not expect the full balance to be called during 2003, it believes such an obligation could be met through a refinancing arrangement or sale of selected assets or a block of insurance business. Regarding the currently scheduled debt repayments, the Company believes its available funds will be adequate to service 2003 debt obligations and, with other available assets, will probably be adequate to service debt obligations through 2004. In addition, the Company's Chairman has expressed potential willingness to loan the Company an additional $3,000,000 if necessary, which could service debt obligations through the majority of 2006. Additional information regarding debt obligations is included in Note 5 of the Notes to Consolidated Financial Statements.

The Company is completing a strategic review of its products and operations. A key element of this initiative is mitigating the significant losses incurred on the Preneed Life business segment and strengthening profitability in the Broker Life and Home Service Life segments.

The Company generated approximately $16,554,000 and $6,394,000 of cash flow from operations during 2002 and 2001, respectively, while using $467,000 of cash from operations in 2000. The 2002 and 2001 increases are principally attributable to growth of Preneed Life premium collections. The 2000 decrease is principally attributable to Federal income tax deposits required early in the year.

Cash used by investment activities of $27,877,000 and $5,555,000 during 2002 and 2001 respectively, relates primarily to investing additional Preneed Life premiums in fixed maturity securities, although the 2002 total also includes investing $11,734,000 of cash and short term balances outstanding at December 31, 2001. Cash provided by investment activities during 2000 of $4,488,000 resulted primarily from a reduction in equity portfolio positions and net cash received from acquisition of the NAIL business, partially offset by additional property and equipment expenditures, including a fractional aircraft ownership share. The $412,000 of cash used by financing activities during 2002 includes $1,317,000 of debt repayments and $956,000 of net withdrawals of policyholder deposits, partially offset by additional borrowings of $2,000,000. Cash used by

financing activities during 2001 includes net withdrawals of policyholder deposits of approximately $1,200,000, debt repayments of $904,000 and common stock repurchases of $396,000. Cash used by financing activities during 2000 includes net withdrawals of policyholder deposits of approximately $1,920,000 and debt repayments of $500,000. The policyholder deposit withdrawals are principally due to the Company's decision not to aggressively compete in crediting higher interest returns on such funds.

The Company is subject to various market risks. However, the most significant such risks relate to fluctuations in prices of equity securities and interest rates. Although the Company experienced negative total returns on its equity portfolio during the past three years, historically these returns have been very favorable and the Company has successfully managed the risk of equity security price fluctuations over many years. As described above, the Company does not anticipate that investment markets will continue to deteriorate at the rate encountered during the past three years. The Company and its investment advisory firm, SMC Advisors, Inc., devote significant attention to the equity markets and reposition the Company's portfolio upon detection of adverse risk trends associated with individual securities or overall markets. SMC Advisors, Inc. also manages market risks associated with investments in option securities, as described in Note 3 of the Notes to Consolidated Financial Statements. The fair

value of the Company's equity portfolio was approximately $7,762,000 and $8,117,000 at December 31, 2002 and 2001, respectively. Accordingly, a 10% decline in equity prices would have reduced the fair value of the Company's equity portfolio by $776,200 and $811,700 at December 31, 2002 and 2001, respectively. The average cost value of the Company's equity portfolio was $6,967,000 and $9,737,000 during 2002 and 2001, respectively.

Regarding interest rate risk, the value of the Company's fixed-maturity investment portfolio will increase or decrease in an inverse relationship with fluctuations in interest rates while net investment income earned on newly-acquired fixed-maturities increases or decreases in direct relationship with interest rate changes. Management estimates that a 100 basis point increase in interest rates ("rate shock") would have decreased the fair value of its $104.0 million fixed maturity portfolio by approximately 3.2% or $3.3 million at December 31. 2002 and 2.8% or $2.2 million at December 31, 2001. From an income perspective, the Company does not believe rising interest rates present a significant risk, as essentially all of the Company's policy liabilities bear fixed rates. However, approximately 45% of policy liabilities contain provisions permitting interest or benefit adjustments at the discretion of the Boards of Directors of the Insurance Subsidiaries. The Company's cash flow testing (described below) indicates that overall profitability will generally be enhanced in rising interest rate scenarios. From a liquidity perspective, the Company's fixed rate policy liabilities have been relatively insensitive to interest rate fluctuations. Accordingly, the Company believes gradual increases in interest rates do not present a significant liquidity exposure. The Company monitors economic conditions on a regular basis and manages this interest rate risk primarily by adjusting the duration of its fixed-maturity portfolio. Historically, the Company has maintained conservative durations in its fixed-maturity portfolio. At December 31, 2002 cash and fixed-maturity investments with maturities of less than five years equaled approximately 60% of total policy liabilities. Notwithstanding the foregoing, if interest rates rise significantly in a short timeframe, there can be no assurance that the life insurance industry, including the Company, would not experience increased levels of surrenders and reduced sales, and thereby be materially adversely affected.

Interest expense on the Company's debt varies quarterly and is therefore also subject to interest rate risk. For its commercial bank debt, the Company elects the lower of the prime lending rate or the one-month LIBOR rate plus 2.75%. For

its related party debt, the interest rate is the higher of 6% or the commercial bank prime lending rate plus 1%. At December 31, 2002, the weighted average rate on the Company's $7,779,168 of borrowings was 4.64%. The Company believes its current liquidity position and profitability levels are adequate to guard against this interest rate risk.

In addition to the measures described above, the Life Insurance Subsidiaries comply with the NAIC promulgated Standard Valuation Law ("SVL") which specifies minimum reserve levels and prescribes methods for determining them, with the intent of enhancing solvency. The SVL also requires the Company to perform annual cash flow testing for its Life Insurance Subsidiaries. This testing is designed to ensure that statutory reserve levels will maintain adequate protection in a variety of potential interest rate scenarios. The Actuarial Standards Board of the American Academy of Actuaries also requires cash flow testing as a basis for the actuarial opinion on the adequacy of the reserves which is a required part of the annual statutory reporting process.

Cash flow testing projects cash inflows from assets and cash outflows for liabilities in various assumed economic and yield curve scenarios. This is a dynamic process, whereby the performance of the assets and liabilities is directly related to the scenario assumptions. (An example would involve the credited interest rate on annuity products and how such rates vary depending upon projected earnings rates, which are based upon asset performance under a particular economic scenario.)

The Life Insurance Subsidiaries' most recent cash flow testing, which was completed in February 2003, involved a review of two basic measures. The first was the value of free market surplus, which is defined as the difference between the projected market value of assets and liabilities at the end of the analysis period (typically 10-20 years). Deficits could indicate the need for corrective action depending upon the severity and the number of scenarios in which a deficit appeared. A second measure involved distributable earnings. Negative earnings for extended durations might impair the ability of the Life Insurance Subsidiaries to continue without exhausting surplus. Again, depending upon severity and frequency, corrective measures might be needed. Based on results of the testing, no corrective measures were indicated at the current time. However, such testing is ongoing and dynamic in nature and future events in the interest and equity markets or a significant change in the composition of Life Insurance Subsidiaries' business could negatively impact testing results and require the initiation of corrective measures.

Any necessary corrective measures could take one or more forms. The duration of existing assets might not match well with those of the liabilities. Certain liabilities, such as those associated with indemnity accident and health, short-term disability and group dental products, are short-term in nature and are best matched with cash and short-term investments. By contrast, whole life insurance, which involves lifetime obligations, is usually best matched by longer duration maturities. In the event there are insufficient assets of these types, a repositioning of the investment portfolio might be undertaken.

Initially balanced durations do not guarantee positive future results. Asset type, quality, and yield will vary depending upon the economic scenario tested. Liabilities will be similarly affected. Projected reinvestment yields may cause overall yields to fall below those required to support projected liabilities. In that event, portfolio realignment might involve the type, quality and yield of investments rather than duration. Alternatively, additional reserve amounts could be allocated to cover any future shortfalls.

The above discussion centers around asset management. Other possible corrective measures might involve liability realignment. The Company's marketing plan could be modified to emphasize certain product types and reduce others. New business

levels could be varied in order to find the optimum level. Management believes that the Company's current liquidity, current bond portfolio maturity distribution and cash flow from operations give it substantial resources to administer its existing business and fund growth generated by direct sales.

FORWARD-LOOKING INFORMATION

All statements, trend analyses and other information contained in this report relative to markets for the Company's products and trends in the Company's operations or financial results, as well as other statements including words such as "anticipate", "believe", "plan", "estimate", "expect", "intend", and other similar expressions, constitute forward-looking statements under the Private Securities Litigation Reform Act of 1995. These forward-looking statements are subject to known and unknown risks, uncertainties and other factors which may cause actual results to be materially different from those contemplated by the forward-looking statements. Such factors include, among other things:

- |X| the market value of the Company's investments, including stock market performance and prevailing interest rate levels (see the Cash Flow and Liquidity section of this Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations);
- |X| customer and agent response to new products, distribution channels and marketing initiatives, including exposure to unrecoverable advanced commissions;
- |X| mortality, morbidity, lapse rates, and other factors which may affect the profitability of the Company's insurance products;
- |X| regulatory changes or actions, including those relating to regulation of insurance products and insurance companies (see the State Insurance Regulation section of Item 1 - Business);
- |X| ratings assigned to the Company and its subsidiaries by independent rating organizations which the Company believes are important to the sale of its products;
- |X| general economic conditions and increasing competition which may affect the Company's ability to sell its products;
- |X| the Company's ability to achieve anticipated levels of operating efficiencies and meet cash requirements based upon projected liquidity sources;
- |X| unanticipated adverse litigation outcomes (see Item 3 - Legal Proceedings); and
- |X| changes in the Federal income tax laws and regulations which may affect the relative tax advantages of some of the Company's products.

There can be no assurance that other factors not currently anticipated by management will not also materially and adversely affect the Company's results of operations.

ITEM 7a. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Quantitative and qualitative disclosures about market risk are described in the Cash Flow and Liquidity section of Item 7 - Management's Discussion and Analysis.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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All other schedules for which provision is made in the applicable accounting regulations of the Securities and Exchange Commission are not required under the related instructions or are inapplicable and therefore have been omitted or the information is presented in the consolidated financial statements or related notes.

REPORT OF INDEPENDENT AUDITORS

The Shareholders and Board of Directors
Citizens Financial Corporation

We have audited the accompanying consolidated balance sheets of Citizens Financial Corporation and subsidiaries at December 31, 2002 and 2001, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2002. Our audits also included the financial statement schedules listed in the Index at Item 15(a). These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Citizens Financial Corporation and subsidiaries at December 31, 2002 and 2001, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

Louisville, Kentucky
March 14, 2003

Citizens Financial Corporation and Subsidiaries
Consolidated Statements of Operations

Year Ended December 31	2002	2001
Revenues:		
Premiums and other considerations	$ 39,722,589	$ 29,969,756
Premiums ceded	(1,243,439)	(1,225,380)
Net premiums earned	38,479,150	28,744,376
Net investment income	5,665,596	6,274,143
Net realized investment gains (losses)	(2,469,768)	(7,911,829)
Other income	427,440	256,229
Total Revenues	42,102,418	27,362,919
Policy Benefits and Expenses:		
Policyholder benefits	19,210,582	17,537,817
Policyholder benefits ceded	(1,340,821)	(1,129,446)
Net benefits	17,869,761	16,408,371
Increase in net benefit reserves	13,226,999	5,846,674
Interest credited on policyholder deposits	781,988	734,687

Commissions	7,394,498	6,414,289
General expenses	6,246,475	6,145,361
Interest expense	305,715	532,962
Policy acquisition costs deferred	(2,712,796)	(3,177,040)
Amortization expense:		
Deferred policy acquisition costs	1,445,740	1,279,485
Value of insurance acquired	560,305	706,773
Goodwill	---	96,013
Depreciation expense	312,793	359,708
Total Policy Benefits and Expenses	45,431,478	35,347,283
Income (Loss) before income tax and cumulative effect of a change in accounting principle	(3,329,060)	(7,984,364)
Income Tax Expense (Benefit)	(757,000)	(2,090,000)
Income (Loss) before cumulative effect of a change in accounting principle	(2,572,060)	(5,894,364)
Cumulative effect - prior years (since January 1, 1999) accounting for embedded options	---	(311,211)
Net Income (Loss)	$(2,572,060)	$(6,205,575)
Per Share Amounts:		
Income (Loss) before cumulative effect of a change in accounting principle	$(1.50)	$(3.39)
Cumulative effect - prior years (since January 1, 1999) accounting for embedded options	---	(0.18)
Net Income (Loss)	$(1.50)	$(3.57)

See Notes to Consolidated Financial Statements.

Citizens Financial Corporation and Subsidiaries
Consolidated Statements of Financial Condition

December 31	2002
ASSETS	
Investments:	
Securities available-for-sale, at fair value:	
Fixed maturities (amortized cost of $101,161,174 and $75,872,277 in 2002 and 2001, respectively)	$ 103,953,815
Equity securities (cost of $7,108,735 and $7,055,402 in 2002 and 2001, respectively)	7,761,892
Investment real estate	3,252,424
Mortgage loans on real estate	---
Policy loans	4,239,128
Short-term investments	632,381
Total Investments	119,839,640

Cash and cash equivalents	6,699,171
Accrued investment income	1,330,036
Reinsurance recoverable	2,886,256
Premiums receivable	215,759
Property and equipment	2,767,763
Deferred policy acquisition costs	9,915,288
Value of insurance acquired	3,617,602
Goodwill	755,782
Federal income tax receivable	250,158
Other assets	164,077
Total Assets	$ 148,441,532

See Notes to Consolidated Financial Statements.

Citizens Financial Corporation and Subsidiaries
Consolidated Statements of Financial Condition

December 31	2002
LIABILITIES	
Policy liabilities:	
Future policy benefits	$ 102,649,565
Policyholder deposits	15,743,293
Policy and contract claims	1,797,195
Unearned premiums	247,625
Other	277,955
Total Policy Liabilities	120,715,633
Note payable - bank	5,779,168
Note payable - related party	2,000,000
Accrued expenses and other liabilities	1,851,467
Deferred federal income tax	234,632
Total Liabilities	130,683,900
COMMITMENTS AND CONTINGENCIES	
SHAREHOLDERS' EQUITY	
Common stock, 6,000,000 shares authorized; 1,686,828 and 1,716,815 shares issued and outstanding in 2002 and 2001, respectively	1,686,828

Additional paid-in capital	7,176,480
Accumulated other comprehensive income	2,223,759
Retained earnings	6,670,565
Total Shareholders' Equity	17,757,632
Total Liabilities and Shareholders' Equity	$148,441,532

See Notes to Consolidated Financial Statements.

Citizens Financial Corporation and Subsidiaries
Consolidated Statements of Shareholders' Equity

	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings
Balance at January 1, 2000	$ 1,767,215	$ 7,736,201	$ 3,322,971	$ 15,210,070
Net Income				238,130
Net unrealized depreciation of available for sale securities			(4,896,265)	
Comprehensive loss				
Common stock repurchases	(9,000)	(95,213)		
Balance at December 31, 2000	$1,758,215	$7,640,988	$(1,573,294)	$15,448,200
Net Loss before cumulative effect of a change in accounting principle				(5,894,364)
Cumulative effect - prior years accounting for embedded options			311,211	(311,211)
Net unrealized appreciation of available for sale securities			3,019,188	
Comprehensive loss				
Common stock repurchases	(41,400)	(355,050)		
Balance at December 31, 2001	$1,716,815	$7,285,938	$1,757,105	$9,242,625
Net Loss				$(2,572,060
Net unrealized appreciation of available for sale securities			466,654	
Comprehensive loss				
Common stock repurchases	(29,987)	(109,458)		

Balance at December 31, 2002	$1,686,828	$7,176,480	$2,223,759	$6,670,565

See Notes to Consolidated Financial Statements.

Citizens Financial Corporation and Subsidiaries
Consolidated Statements of Cash Flows

Year Ended December 31	2002	2001
Cash Flows from Operations:		
Net income (loss)	$ (2,572,060)	$ (6,205,575
Adjustments reconciling to cash from operations:		
Increase in benefit reserves	13,296,995	5,979,218
Increase (decrease) in claim liabilities	354,839	(374,591
(Increase) decrease in reinsurance recoverable	(130,576)	(68,933
Interest credited on policyholder deposits	781,762	734,687
Provision for amortization and depreciation, net of deferrals	(393,958)	(735,061
Amortization of premium and accretion of discount on securities purchased, net	26,712	(138,180
Net realized investment (gains) losses	2,469,768	7,911,829
(Increase) decrease in accrued investment income	60,514	(62,060
Change in other assets and liabilities	468,709	(391,533
Deferred income tax expense (benefit)	(413,000)	923,000
(Increase) decrease in federal income taxes receivable	2,604,775	(1,490,431
Cumulative effect - change in accounting principle	---	311,211
Net Cash provided by (used in) Operations	16,554,480	6,393,581
Cash Flows from Investment Activities:		
Securities available-for-sale:		
Purchases - fixed maturities	(69,026,797)	(18,440,196
Purchases - equity securities	(13,333,227)	(13,909,021
Sales - fixed maturities	43,724,194	13,210,562
Sales - equity securities	10,922,498	13,829,235
Investment management and brokerage account fees	(48,716)	(177,786
Short-term investments sold (acquired), net	19,811	(41,813
Additions to real estate	---	(154,262
Additions to property and equipment, net	(31,908)	(40,392
Net cash received for insurance business and subsidiary acquisitions	---	---
Other investing activities, net	(102,479)	168,763
Net Cash provided by (used in) Investment Activities	(27,876,624)	(5,554,910
Cash Flows from Financing Activities:		
Policyholder deposits	741,863	1,006,892
Policyholder withdrawals	(1,698,063)	(2,205,095
Proceeds from additional borrowings	2,000,000	---
Payments on notes payable - bank	(1,316,666)	(904,166
Repurchase of common stock	(139,445)	(396,450
Repayment of brokerage advances	---	---
Net Cash used in Financing Activities	(412,311)	(2,498,819

Net Increase (Decrease) in Cash and Cash Equivalents	(11,734,455)	(1,660,148
Cash and Cash Equivalents at Beginning of Period	18,433,626	20,093,774
Cash and Cash Equivalents at End of Period	$ 6,699,171	$ 18,433,626

See Notes to Consolidated Financial Statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1--NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Presentation. The accompanying consolidated financial statements include the accounts of Citizens Financial Corporation and its wholly owned subsidiaries: Citizens Security Life Insurance Company ("Citizens Security"), United Liberty Life Insurance Company ("United Liberty"), Citizens Insurance Company ("Citizens Insurance"), and Corporate Realty Service, Inc. ("Corporate Realty"). These entities are collectively hereinafter referred to as the "Company". United Liberty, and (effective January 31, 2001) Citizens Insurance, are also wholly owned subsidiaries of Citizens Security. All significant intercompany accounts and transactions are eliminated in consolidation. Certain balances in prior years have been reclassified to conform to current year classifications.

Nature of Operations. The Company engages primarily in the business of life insurance, annuities and accident and health insurance through Citizens Security and United Liberty ("the Life Insurance Subsidiaries"). The Life Insurance Subsidiaries offer life, fixed-rate annuity and accident and health insurance products to individuals and groups through independent agents. Citizens Insurance was acquired during 1999 (see Note 2) and is licensed as a property and casualty insurer in four states. The Company is planning to offer home service fire and casualty insurance coverage; however, Citizens Insurance currently has no business inforce. Corporate Realty manages the Company's real estate along with two other properties affiliated with the Company's Chairman.

The individual life insurance products currently offered by the Life Insurance Subsidiaries consist of traditional whole life insurance and universal life insurance policies. Citizens Security also sells group life and accidental death and dismemberment policies. The fixed-rate annuity products offered by Citizens Security consist of flexible premium deferred annuities, life policy annuity riders, and single premium deferred annuities. Citizens Security's individual accident and health insurance products provide coverage for monthly income during periods of hospitalization, scheduled reimbursement for specific hospital and surgical expenses and cancer treatments, and lump sum payments for accidental death or dismemberment, while the group accident and health products provide coverage for short and long-term disability, income protection and dental procedures.

Citizens Security is licensed to sell products in the District of Columbia and 20 states primarily located in the South and Southeast. United Liberty is licensed to sell products in 23 states primarily located in the South, Midwest, and West. United Liberty's ongoing sales efforts are focused primarily in nine states where Citizens Security is not licensed.

The Life Insurance Subsidiaries market their portfolio of products through the personal producing general agent distribution system and presently have approximately 3,500 sales representatives. Many of these also represent other

insurance carriers. Approximately 600 of the agents specialize in the home service market while approximately 800 are Preneed representatives who market through funeral homes. These markets consist primarily of individuals who desire whole life policies with policy limits typically below $10,000.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Investments. The Company classifies fixed maturities and equity securities as "available-for-sale". Available-for-sale securities are carried at fair value, with unrealized gains and losses included in accumulated other comprehensive income (loss), net of applicable deferred taxes and adjustments to related deferred policy acquisition costs. Mark-to-market accounting is used for equity options embedded in convertible bonds and all other derivatives. Changes in the fair value of derivatives are reported currently as realized gains or losses.

We periodically evaluate whether the declines in fair value of our investments are other-than-temporary. Our evaluation consists of a review of qualitative and quantitative factors, including analysis of the company's competitive position in its markets, deterioration in the financial condition of the issuer, downgrades of the security by a rating agency, and other publicly available issuer-specific news or general market conditions. For investments in companies with no quoted market price, we consider similar qualitative and quantitative factors and also take into account the cost of the investment, the type of investment, subsequent purchases of the same or similar investments, the current financial position and operating results of the company invested in, and such other factors as may be relevant. Declines in fair values of securities deemed to be other-than-temporary are included in net income as realized investment losses. Determining what constitutes an other-than-temporary decline involves

significant judgment. Declines in fair value below cost not considered other-than-temporary in the current period could be considered other-than-temporary in a future period and reduce earnings to the extent of the write-down.

For purposes of computing realized gains and losses on fixed maturities and equity securities sold, the carrying value is determined using the specific-identification method. Mortgage loans and policy loans are carried at unpaid balances. Investment real estate is carried at depreciated cost. Short-term investments, which consist of certificates of deposit and treasury bills, are carried at cost which approximates fair value. Cash and cash equivalents consist of highly liquid investments with maturities of three months or less at the date of purchase and are also carried at cost which approximates fair value.

Deferred Policy Acquisition Costs. Commissions and other policy acquisition costs which vary with, and are primarily related to, the production of new insurance contracts are deferred, to the extent recoverable from future policy revenues and gross profits, and amortized over the life of the related contracts. See Premiums, Benefits and Expenses regarding amortization methods.

Property and Equipment. Property and equipment, including the home office building, are carried at cost less accumulated depreciation, using principally the straight-line method of depreciation. Accumulated depreciation at December 31, 2002 was $2,361,180 ($2,333,330 at December 31, 2001).

Goodwill and Value of Insurance Acquired. Goodwill represents the excess of purchase price of purchased subsidiaries, over amounts assigned (based on estimated fair values at the date of acquisition) to the identifiable net assets acquired. Effective January 1, 2002, the Company discontinued amortizing goodwill and began testing for potential impairment of goodwill on an annual basis. Prior to 2002, the Company amortized goodwill over 10 to 20 years using the straight-line method. At December 31, 2002 and 2001, accumulated amortization was $412,861.

Value of insurance acquired is recorded for the estimated value assigned to the insurance in force of the purchased subsidiaries at the dates of acquisition. The assigned value is amortized over the expected remaining life of the insurance in force using methods consistent with that used for amortization of policy acquisition costs (as described under Premiums, Benefits and Expenses). At December 31, 2002, accumulated amortization was $5,678,772 ($5,118,467 at December 31, 2001).

Benefit Reserves and Policyholder Deposits. Traditional life and accident and health insurance products include those contracts with fixed and guaranteed premiums and benefits and consist principally of whole-life and term insurance policies, limited-payment life insurance policies and certain annuities with life contingencies. Reserves on such policies are based on assumed investment yields which range from 6% to 7%. Reserves on traditional life and accident and health insurance products are determined using the net level premium method based on future investment yields, mortality, withdrawals, and other assumptions, including dividends on participating policies. Such assumptions are based on past experience and include provisions for possible unfavorable deviation.

Benefit reserves and policyholder contract deposits on universal life, other interest-sensitive life products and investment-type products are determined using the retrospective deposit method and consist of policy account balances, before deducting surrender charges, which accrue to the benefit of the policyholder.

Participating insurance business constituted approximately 6% of ordinary life insurance inforce at December 31, 2002, 2001 and 2000, and 1%, 4%, and 4% of annualized ordinary life premium inforce at December 31, 2002, 2001, and 2000, respectively. Participating dividends are determined at the discretion of the Board of Directors.

Reserves on insurance policies acquired by purchase are based on assumptions considered appropriate as of the date of purchase. Assumed investment yields for such acquired policies range from 5.5% to 9.0%.

Premiums, Benefits and Expenses. Premiums for traditional individual life (including Preneed) and accident and health policies are reported as earned when due. Benefit claims (including an estimated provision for claims incurred but not reported), benefit reserve changes and expenses (except those deferred) are charged to expense as incurred. Deferred policy acquisition costs related to traditional life and accident and health policies are charged to expense over the life of the policy using methods and assumptions consistent with those used in estimating liabilities for future policy benefits. In determining whether a premium deficiency exists on short-duration policies, management does not give consideration to investment income.

Revenues for universal life and investment-type products consist of investment income and policy charges for the cost of insurance, policy initiation, administrative surrender fees and investment income. Expenses include interest

credited to policy account balances, incurred administrative expenses and benefit payments in excess of policy account balances. Deferred policy acquisition costs related to universal life and investment-type products are amortized in relation to the incidence of expected gross profits over the life of the policies. Expected gross profits are reviewed at each reporting period, and to the extent actual experience varies from that previously assumed, the effects of such variances are recorded in the current period.

Liabilities for Policy Claims. Policy claim liabilities are based on known liabilities plus estimated future liabilities developed from trends of historical data applied to current exposures. These liabilities are closely monitored and adjustments for changes in experience are made in the period identified.

Federal Income Taxes. The Company uses the liability method of accounting for income taxes. Deferred income taxes are provided for cumulative temporary differences between balances of assets and liabilities determined under GAAP and balances determined for tax reporting purposes.

Earnings Per Share. Basic earnings per share amounts are based on the weighted average number of common shares outstanding during the year.

Note 2--ACQUISITIONS

On July 7, 2000, the Company acquired, through an assumption reinsurance agreement, 100% of the inforce business of National Affiliated Investors Life Insurance Company ("NAIL") for a net cash purchase price of approximately $355,000. The acquisition was coordinated through the National Organization of Life and Health Guaranty Associations. The acquired business consisted primarily of individual life insurance with policy reserves and annual premium of approximately $3,500,000 and $300,000, respectively.

On October 14, 1999, the Company acquired 100% of the stock of Citizens Insurance (formerly Kentucky Insurance Company) from an unaffiliated insurance holding company (the "Citizens Insurance Acquisition"). Citizens Insurance is licensed as a property and casualty insurance company in four states and has approximately $3.6 million of statutory capital and surplus; however, it currently has no insurance operations. The aggregate purchase price for the Citizens Insurance Acquisition was approximately $3,550,000 (including net costs associated with the acquisition of approximately $50,000).

Note 3--INVESTMENTS

The cost and fair value of investments in fixed maturities and equity securities are shown below. The cost amounts are adjusted for amortization of premium and accretion of discount on fixed maturities and for write-downs of securities whose decline in value is believed to be other than temporary.

December 31, 2002	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	(Ca
Fixed Maturities:				
U.S. Government obligations	$ 39,440,067	$ 1,241,430	$ 7,864	
Corporate securities	51,650,022	1,876,778	683,232	
Mortgage-backed securities	10,071,085	371,403	5,874	
Total	$101,161,174	$ 3,489,611	$ 696,970	

Equity Securities	$ 7,108,735	$ 845,055	$ 191,898	$

December 31, 2001

Fixed Maturities:				
U.S. Government obligations	$ 26,038,744	$ 637,535	$ 95,265	$
Corporate securities	47,435,636	1,341,524	366,107	
Mortgage-backed securities	2,397,897	144,637	85	
Total	$ 75,872,277	$ 2,123,696	$ 461,457	
Equity Securities	$ 7,055,402	$ 1,243,333	$ 181,777	$

The fair values for investments in fixed maturities and equity securities are based on quoted market prices, where available. For investments in fixed maturities and equity securities not actively traded, fair values are estimated using values obtained from independent pricing services.

The annual change in net unrealized investment appreciation or depreciation, at December 31, 2002, 2001 and 2000, and the amount of net realized investment gain or loss included in net income for the respective years then ended are shown below. The 2002 change in net unrealized appreciation for fixed maturities shown below is after recognizing the January 1, 2001 pretax transition adjustment of approximately $471,532, as described in Note 16.

Year Ended December 31	2002	2001	
Fixed maturities:			
Change in net unrealized appreciation	$ 1,130,402	$ 2,303,205	$(1
Net realized gain (loss)	$ (228,710)	$(1,260,092)	$ 1
Equity securities:			
Change in net unrealized appreciation	$ (408,399)	$ 2,160,985	$(5
Net realized gain (loss)	$(2,241,058)	$(6,651,737)	$

The amortized cost and fair value of investments in fixed maturities at December 31, 2002, by contractual maturity are shown below. Expected maturities for investments in fixed maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations, sometimes without prepayment penalties.

December 31, 2002	Amortized Cost	Fair Value
Due in one year or less	$ 14,753,468	$ 14,881,072
Due after one year through five years	49,355,130	50,889,915
Due after five years through ten years	17,894,409	18,475,601
Due after ten years	9,087,082	9,270,613
Subtotal	91,090,089	93,517,201

Mortgage-backed securities	10,071,085	10,436,614
Total	$ 101,161,174	$ 103,953,815

Gross gains of $555,169, $463,679, and $2,268,554 and gross losses of $819,705, $1,778,519, and $1,127,299 were realized on the sale of available-for-sale fixed maturities during 2002, 2001, and 2000, respectively. Included in gross realized losses during 2002, 2001, and 2000 are net adjustments to the carrying value of available-for-sale fixed maturities of $501,399, $739,000, and $912,000 respectively, relating to declines in value which were considered by management to be other than temporary. Net realized gains from the sale of fixed maturities have been increased (decreased) by $35,826, $63,492, and $(80,166) in 2002, 2001, and 2000 respectively, due to amortization of deferred policy acquisition costs. In addition, net realized gains from the sale of fixed maturities have been reduced by $8,744 in 2001 for incentive fees earned by the portfolio manager.

Gross gains of $1,814,053, $1,378,585, and $16,764,844 and gross losses of $4,093,424, $8,245,943, and $16,740,314 were realized on the sale of available-for-sale equity securities during 2002, 2001 and 2000. Included in gross realized losses during 2002, 2001, and 2000 are adjustments to the carrying value of available-for-sale equity securities of $753,953, $1,533,000, and $5,733,000 respectively, relating to declines in value which were considered by management to be other than temporary. Net realized gains from the sale of equity securities have been increased by $47,936, $252,534, and $302,629 in 2002, 2001, and 2000 respectively, due to amortization of deferred policy acquisition costs. In addition, net realized gains from the sale of available-for-sale equity securities have been reduced by $9,623, $36,913, and $207,369 in 2002, 2001, and 2000, respectively, for incentive and management fees earned by the portfolio manager.

Net unrealized appreciation of available-for-sale securities is summarized as follows:

December 31	2002	20
Net appreciation on available-for-sale:		
Fixed maturities	$2,792,641	$1,662,2
Equity securities	653,157	1,061,5
Adjustment of deferred policy acquisition costs	(76,468)	(61,5
Deferred income taxes	(1,145,571)	(905,1
Net unrealized appreciation	$2,223,759	$1,757,10

Investment management services are provided by a firm affiliated with certain board members and shareholders of the Company - see Note 15 - Related Party Transactions.

Major categories of investment income are summarized as follows:

Year Ended December 31	2002	2001	2

Fixed maturities	$ 4,985,779	$ 4,785,712	$ 4,410,
Equity securities	269,695	284,922	397,
Investment real estate	223,822	239,762	107,
Mortgage loans on real estate	9,328	14,033	14,
Policy loans	254,693	258,135	239,
Short-term investments and other	216,602	1,014,971	1,138,
Subtotal	5,959,919	6,597,535	6,308,
Investment expense	(294,323)	(323,392)	(315,
Net investment income	$ 5,665,596	$ 6,274,143	$ 5,993,

The Company limits credit risk by diversifying its investment portfolio among government and corporate fixed maturities and common and preferred equity securities. It further diversifies these investment portfolios within industry sectors. As a result, management believes that significant concentrations of credit risk do not exist. The following are the only investments (other than the U.S. Governments) comprising more than ten percent of shareholders' equity at December 31, 2002: Clear Channel Communications ($2,977,500), JP Morgan ($2,235,973), and Preferred Term Securities III, Ltd. ($1,952,556). At December 31, 2002, the Company had no investments which had not been income producing for a period of at least twelve months prior to year-end and had approximately $170,000 of fixed maturity securities on non-accrual status at December 31, 2002.

The following table is a reconciliation of the net unrealized gain (loss) arising during the period and the change in net unrealized gains (losses) as reported on the accompanying statements of shareholders' equity.

Year Ended	Pretax Amount	Tax Expense	Net-of-Ta Amount
December 31, 2002:			
Unrealized loss	$(1,762,718)	$ (599,325)	$(1,163,
Less: Reclassification adjustment for losses realized in net income	(2,469,768)	(839,721)	(1,630,
Change in net unrealized loss	$ 707,050	$ 240,396	$ 466,
December 31, 2001:			
Unrealized loss	$(3,593,744)	$(1,391,125)	$(2,202,
Less: Reclassification adjustment for gains realized in net income	(7,911,829)	(2,690,022)	(5,221,
Change in net unrealized loss	$4,318,085	$1,298,897	$3,019,

As an income generation strategy, the Company takes certain option positions, generally on equity securities or related market indices and on equity options embedded in convertible bonds. Although such positions may be covered by actual securities owned or offsetting options, hedge accounting is not used.

Accordingly, all such positions are marked to market and changes in value reported as realized gains or losses. During 2002, option purchases totaled approximately $822,000 and related net realized gains totaled approximately $63,000. At December 31, 2002 net option positions outstanding had a market value of $60,000, with an associated 2002 realized loss recorded of $36,000. Approximately $7,000 of these positions contain market risk of loss beyond the recorded value.

Pursuant to requirements of certain state insurance departments, the Company has investments with a carrying value of $52,701,872, at December 31, 2002, placed on deposit at various financial institutions which are restricted from withdrawal without prior regulatory approval.

The Company owns the building and land which it currently occupies. At December 31, 2002 and 2001, the Company occupied approximately 31% and 29% respectively, of the building with the remaining space leased or available for lease to third-party tenants. The accompanying financial statements reflect the proportionate Company occupied share of the building and related operating expense as property and equipment and general expense, respectively. The remaining portion is reflected as investment real estate and as a reduction of investment income, respectively. Accumulated depreciation at December 31, 2002 and 2001 on the investment real estate portion of the building was $1,153,634 and $1,041,432, respectively.

The Company leases office space to third-party tenants under noncancellable lease agreements. Future minimum rental income is $527,000, $373,000, $287,000, $64,000 and $6,000 for years 2003 through 2007, respectively.

Note 4--VALUE OF INSURANCE ACQUIRED

The value of insurance acquired is an asset which represents the present value of future profits on business acquired, using interest rates of 6.6% to 9%. Balances outstanding relate primarily to the purchase of United Liberty and two additional companies which have been merged into Citizens Security (Integrity National Life Insurance Company and Old South Life Insurance Company) along with the NAIL total of $355,360 added during 2000. An analysis of the value of insurance acquired for the years ended December 31, 2002, 2001 and 2000 is as follows:

Year Ended December 31	2002	2001	2000
Balance at beginning of year	$4,177,907	$4,884,680	$5,295,818
Business acquired	---	---	355,360
Accretion of interest	253,996	296,964	312,002
Amortization	(814,301)	(1,003,737)	(1,078,500)
Balance at end of year	$3,617,602	$4,177,907	$4,884,680

Amortization of the value of insurance acquired (net of interest accretion) in each of the following five years will be approximately: 2003 - $480,000; 2004 - $423,000; 2005 - $382,000; 2006 - $338,000, and 2007 - $298,000.

Note 5--DEBT

Debt consists of the following:

December 31	2002	2001

Commercial bank, due 2007	$ 5,779,168	$ 7,095,834
Related party, due 2007	2,000,000	---
Total	$7,779,168	$7,095,834

The Company's outstanding commercial bank borrowings relate primarily to various insurance company acquisitions. Interest is payable quarterly at the lower of the bank's prime lending rate or the one month LIBOR rate plus 2.75%. Scheduled principal installments are due as follows: 2003 and 2004 - $1,316,667; 2005 and 2006 - $1,416,666; and 2007 - $312,502. However, the loan agreement for the bank notes contains covenants regarding asset acquisitions, shareholder equity and dividends, and maintenance of a debt to earnings ratio. Due to losses incurred during 2002, the Company did not meet one of the covenants (debt to earnings ratio), although the lender has waived this covenant violation through December 31, 2002. Since the Company is not assured of meeting this covenant throughout 2003, the full loan balance of $5,779,168 can be considered payable within one year. Although the Company does not expect the full balance to be called during 2003, it believes such an obligation could be met through a refinancing arrangement or sale of selected assets or a block of insurance business. The Company has pledged the issued and outstanding common and preferred stock of Citizens Security as collateral for the commercial bank notes.

During 2002, the Company borrowed $2,000,000 from its Chairman. These funds were used to purchase redeemable preferred stock of the Company's subsidiary, Citizens Security, thereby strengthening the statutory capital and surplus of Citizens Security. Interest on the debt is payable quarterly by the Company at an annual rate equal to the greater of 6.00% or the prime lending rate plus 1%. The outstanding principal is callable upon 90 days notice or otherwise due on June 30, 2005, except however, under terms of a subordination agreement between the Chairman and the Company's commercial bank, repayment is prohibited until all outstanding commercial bank borrowings are repaid.

Cash paid for interest on debt was $412,719, $635,594, and $771,095 during 2002, 2001 and 2000, respectively.

Note 6--EARNINGS AND DIVIDENDS PER SHARE

The following table sets forth the computation of earnings (losses) per share. No dividends were paid or accrued for 2002, 2001, or 2000.

December 31	2002	20
Numerators:		
Income (Loss) before cumulative effect of a change in accounting principle	$(2,572,060)	$(5,894,3
Cumulative effect of a change in accounting principle	---	(311,2
Net Income (Loss)	$(2,572,060)	$(6,205,5
Denominator:		
Weighted average common shares	1,711,627	1,740,
Earnings (Loss) Per Share:		
Income (Loss) before cumulative effect of a change in accounting principle	$(1.50)	$(3.
Cumulative effect of a change in accounting principle	---	(0.

Net Income (Loss)	$(1.50)	$(3.

Note 7--INCOME TAXES

Income taxes consist of the following:

December 31	2002	2001	2000
Current tax expense (benefit)	$(344,000)	$(3,013,000)	$1,755,000
Deferred tax expense (benefit)	(413,000)	923,000	(1,545,000)
Income tax expense (benefit)	$(757,000)	$(2,090,000)	$ 210,000

Tax expense includes a current state and local income tax provision (benefit) of $(36,000), $(230,000), and $350,000 in 2002, 2001, and 2000 respectively. Deferred income taxes are provided for cumulative temporary differences between balances of assets and liabilities determined under GAAP and balances determined for tax reporting purposes.

Significant components of the Company's deferred tax liabilities and assets as of December 31, 2002 and 2001 are as follows:

December 31	2002	20
Deferred Tax Liabilities:		
Value of insurance acquired	$ 1,229,985	$ 1,420,4
Deferred policy acquisition costs	1,922,754	1,487,2
Net unrealized gains on available-for-sale securities	1,145,571	905,1
Other	635,594	550,5
Total deferred tax liabilities	4,933,904	4,363,5
Deferred Tax Assets:		
Policy and contract reserves	3,343,789	2,676,6
Fixed maturities and equity securities	912,329	1,161,5
Real estate	548,668	548,6
Alternative minimum tax credit carryforwards	201,918	196,7
Net operating and capital loss carryforwards	707,298	82,4
Other	256,767	248,0
Total deferred tax assets	6,039,991	4,914,0
Valuation allowance for deferred tax assets	(1,374,497)	(1,060,7
Net deferred tax assets	4,596,272	3,853,2
Net deferred tax assets (liabilities)	$ (337,632)	$ (510,2

The following is a reconciliation of income tax expense at the federal statutory

rate, to the tax at the Company's effective income tax rate:

December 31	2002	2001	2000
Tax at the statutory rate	$ (1,132,000)	$ (2,714,700)	$ 152,400
Change in valuation allowance	314,000	(358,500)	585,800
Small life deduction	106,000	1,141,100	(276,300)
State and local income tax	(36,000)	(165,200)	233,600
Surtax exemption and other	(2,000)	24,000	(446,100)
Dividend exclusion	(7,000)	(16,700)	(39,400)
Tax at the effective rate	$ (757,000)	$ (2,090,000)	$ 210,000

Income taxes paid (refunded) in 2002, 2001, and 2000 were $(3,065,000), $(1,293,000), and $3,100,000, respectively. The Company has $328,000 of net operating loss carryforwards and $1,752,000 of capital loss carryforwards which expire in years 2016 and 2017. The change in the valuation allowance is due principally to the limitation in the recovery of prior year taxes at the full statutory rate.

Under the tax law in effect prior to 1984, a portion of income of Citizens Security was not taxed when earned. It was accumulated in a tax account known as policyholders' surplus. Under the provisions of the Deficit Reduction Act of 1984, policyholders' surplus accounts were frozen at their December 31, 1983 balance of $859,000 for Citizens Security on a merged basis. Distributions from the policyholders' surplus would be subject to income tax. At December 31, 2002, Citizens Security could have paid additional dividends of approximately $22,400,000 before paying tax on any part of its policyholders' surplus accounts. No provision has been made for the related deferred income taxes which total $292,000, based on current tax rates as of December 31, 2002.

Note 8--STATUTORY ACCOUNTING PRACTICES AND SHAREHOLDERS' EQUITY

The Insurance Subsidiaries are domiciled in Kentucky and prepare their statutory-basis financial statements in accordance with statutory accounting practices ("SAP") prescribed or permitted by the Kentucky Department of Insurance ("KDI"). "Prescribed" statutory accounting practices include state insurance laws, regulations, and general administrative rules, as well as a variety of publications of the National Association of Insurance Commissioners ("NAIC"). "Permitted" statutory accounting practices encompass all accounting practices that are not prescribed; such practices may differ from state to state, may differ from company to company within a state, and may change in the future. Effective January 1, 2001, the NAIC revised its Accounting Practices and Procedures Manual in a process referred to as Codification. The KDI has adopted the revised manual, which has changed, to some extent, prescribed statutory accounting practices which the Insurance Subsidiaries use to prepare their statutory-basis financial statements. The primary statutory changes affecting the Insurance Subsidiaries are, establishment of deferred income taxes, recognizing as realized losses securities impairments considered other than temporary, recording an allocable share of the Company's accrued employee benefit obligations, and revision of the statutory equity method of accounting which now precludes a parent insurer from recording as income, its share of undistributed subsidiary earnings. Effective January 1, 2001, the Insurance Subsidiaries recorded a net deferred tax benefit from Codification of $1,750,000, partially offset by approximately $228,000 of accrued employee benefit obligations.

Statutory-basis net income and capital and surplus for the Company's combined insurance operations, for the three years ended December 31, 2002 are shown below. These amounts are combined totals for Citizens Security, United Liberty, and Citizens Insurance, with adjustments to eliminate intercompany holdings and

activity.

December 31	2002	2001	2000
Net Income (Loss)	$ (1,663,236)	$ (3,762,603)	$ 1,961,792
Capital and Surplus	$ 9,903,639	$ 9,687,289	$ 11,694,494

Principal differences between SAP and GAAP include: a) costs of acquiring new policies are generally deferred and amortized for GAAP; b) value of insurance inforce acquired is established as an asset for GAAP; c) benefit reserves are calculated using more realistic investment, mortality and withdrawal assumptions for GAAP; d) the change in SAP deferred income taxes associated with timing differences is recorded directly to equity rather than as a component of net

income as required for GAAP; e) assets and liabilities of acquired companies are adjusted to their fair values at acquisition with the excess purchase price over such fair values recorded as goodwill under GAAP; f) available-for-sale fixed maturity investments are reported at fair value with unrealized gain and losses reported as a separate component of shareholders' equity for GAAP; and g) statutory asset valuation reserves and interest maintenance reserves are not required for GAAP.

Statutory restrictions limit the amount of dividends which the insurance companies may pay. Generally, dividends during any year may not be paid, without prior regulatory approval, in excess of the lesser of (a) 10% of statutory shareholder's surplus as of the preceding December 31, or (b) statutory net operating income for the preceding year. During 2002, the Company purchased $2,000,000 of redeemable preferred stock from Citizens Security, as further described in Note 5. During 2001, the Company contributed the stock of Citizens Insurance and $150,000 to Citizens Security. The statutory value of the contributed Citizens Insurance stock was $3,540,555. Citizens Security contributed the $150,000 received from the Company to Citizens Insurance. During 2000, with appropriate prior regulatory approval, Citizens Security redeemed $1,200,000 of its outstanding preferred stock from the Company. United Liberty paid dividends to Citizens Security of $214,000, $292,000 and $200,000 during 2002, 2001, and 2000 respectively. The Insurance Subsidiaries must each maintain $1,250,000 of capital and surplus, the minimum required for insurance companies domiciled in Kentucky. The KDI imposes minimum risk-based capital ("RBC") requirements on insurance enterprises that were developed by the NAIC. The formulas for determining the amount of RBC specify various weighting factors that are applied to financial balances and various levels of activity based on the perceived degree of risk. Regulatory compliance is determined by a ratio (the "Ratio") of the enterprise's regulatory total adjusted capital, as defined by the NAIC, to its required authorized control level RBC, as defined by the NAIC. Enterprises below specific trigger points or ratios are classified within certain levels, each of which requires specified corrective action. Based on RBC computations as of December 31, 2002, the Insurance Subsidiaries each have statutory capital which is well in excess minimum regulatory requirements.

Note 9--SEGMENT INFORMATION

The Company's operations are managed along five principal insurance product lines: Home Service Life, Broker Life, Preneed Life, Dental, and Other Health. Products in all five lines are sold through independent agency operations. Home Service Life consists primarily of traditional life insurance coverage sold in amounts of $10,000 and under to middle and lower income individuals. This distribution channel is characterized by a significant amount of agent contact with customers throughout the year. Broker Life product sales consist primarily of simplified issue and graded-benefit policies in amounts of $10,000 and under.

Other products in this segment which are not aggressively marketed include: group life, universal life, annuities and participating life coverages. Preneed Life products are sold to individuals in connection with prearrangement of their funeral and include single premium and multi-pay policies with coverages generally in amounts of $10,000 and less. These policies are generally sold to older individuals at increased premium rates. Dental products are term coverages generally sold to small and intermediate size employer groups. Other Health products include various accident and health coverages sold to individuals and employer groups.

Segment information as of December 31, 2002, 2001 and 2000, and for the years then ended is as follows:

December 31	2002	2001	2000
Revenue:			
Home Service Life	$ 9,260,097	$ 9,290,120	$ 9,036,005
Broker Life	5,964,089	6,497,286	6,328,884
Preneed Life	19,706,136	9,974,405	5,345,930
Dental	8,209,257	8,025,375	7,933,598
Other Health	1,432,607	1,487,562	1,469,316
Segment Totals	44,572,186	35,274,748	30,113,733
Net realized investment gains (losses)	(2,469,768)	(7,911,829)	1,180,879
Total Revenue	$42,102,418	$27,362,919	$31,294,612

Below are the net investment income amounts which are included in the revenue totals above.

Year Ended December 31	2002	2001	2000
Net Investment Income:			
Home Service Life	$ 1,790,949	$ 2,053,995	$ 2,028,680
Broker Life	2,178,667	2,579,117	2,538,610
Preneed Life	1,592,356	1,514,638	1,298,434
Dental	24,896	35,312	39,289
Other Health	78,728	91,081	88,349
Segment Totals	$ 5,665,596	$ 6,274,143	$ 5,993,362

The Company evaluates performance based on several factors, of which the primary financial measure is segment profit. Segment profit represents pretax earnings, determined in accordance with the accounting policies described in Note 1, except net realized investment gains and interest expense are excluded. A significant portion of the Company's realized investment gains and losses are generated from investments in equity securities.

Year Ended December 31	2002	2001	
Segment Profit (Loss):			
Home Service Life	$275,809	$ 382,723	$
Broker Life	(265,488)	74,960	
Preneed Life	(670,349)	(264,488)	
Dental	297,740	256,385	
Other Health	(191,289)	10,847	

Segment Totals	(553,577)	460,427	
Net realized investment gains (losses)	(2,469,768)	(7,911,829)	1
Interest expense	305,715	532,962	
Income (Loss) before income tax and cumulative effect of a change in accounting principle	$ (3,329,060)	$ (7,984,364)	$

Depreciation and amortization amounts below consist of amortization of the value of insurance acquired, deferred policy acquisition costs and goodwill, along with depreciation expense.

December 31	2002	2001	2000
Depreciation and Amortization:			
Home Service Life	$ 750,811	$ 873,529	$ 723,255
Broker Life	482,049	678,446	506,016
Preneed Life	983,848	779,199	350,758
Dental	61,480	68,866	61,286
Other Health	40,650	41,939	45,888
Segment Totals	$ 2,318,838	$ 2,441,979	$ 1,687,203

Segment asset totals are determined based on policy liabilities outstanding in each segment.

December 31	2002	2001	2000
Assets:			
Home Service Life	$ 45,219,971	$ 44,818,038	$ 45,577,255
Broker Life	53,874,949	54,954,194	57,721,008
Preneed Life	46,739,831	34,138,535	29,421,677
Dental	660,334	726,728	799,496
Other Health	1,946,447	1,959,588	2,018,570
Total Assets	$148,441,532	$136,597,083	$135,538,006

Note 10--QUARTERLY FINANCIAL DATA (Unaudited)

Below is selected consolidated quarterly financial data for each of the two years ended December 31, 2002.

Year 2002 - Quarter	1	2	3	4
Segment Revenue	$ 9,776,888	$ 11,018,089	$ 12,427,634	$ 11,34
Investment gains (losses), net	(328,734)	(1,468,150)	(701,218)	2
Total Revenue	9,448,487	9,549,939	11,726,416	11,37
Segment Profit (Loss)	(57,314)	(646,672)	90,388	6
Investment gains (losses), net	(328,401)	(1,468,150)	(701,218)	2
Interest expense	81,228	78,176	74,649	7

Income tax expense (benefit)	(70,000)	(345,000)	(213,000)	(12
Net Income (Loss)	$ (396,943)	$ (1,847,998)	$ (472,479)	$ 14
Net Income (Loss) Per Share	$ (0.23)	$ (1.08)	$ (0.27)	$

Year 2001 - Quarter:	1*	2*	3*	4
Segment Revenue	$ 8,453,433	$ 8,935,430	$ 9,039,850	$ 8,84
Investment gains (losses), net	171,896	(3,469,996)	(3,100,898)	(1,51
Total Revenue	$ 8,625,329	$ 5,465,434	$ 5,938,952	$ 7,33
Segment Profit (Loss)	$ 328,901	$ (99,095)	$ 132,237	$ 9
Investment gains (losses), net	171,896	(3,469,996)	(3,100,898)	(1,51
Interest expense	171,651	143,050	127,504	9
Income tax expense (benefit)	86,000	(972,000)	(810,000)	(39
Net Income (Loss) before cumulative effect of change in accounting	243,146	(2,740,141)	(2,286,165)	(1,11
Cumulative effect from prior years' of accounting for embedded options	(311,211)	---	---	
Net Loss	$ (68,065)	$(2,740,141)	$(2,286,165)	$(1,11
Net Loss Per Share	$ (0.04)	$ (1.57)	$ (1.32)	$

* Net Loss for the quarters ended March 31, June 30, and September 30, 2001 has been restated from amounts previously reported in the Company's Form 10-Qs. The restated amounts reflect correction of policy benefit reserves and related deferred acquisition costs for the Preneed Life segment. In addition, corresponding income taxes have been revised for the Preneed Life change and to reflect the actual effective tax rate applicable for the year. The effect of the restatement for the first three quarters of 2001 was to increase earnings and per share amounts (i.e. decrease Net Loss) as follows:

2001 Revisions	Pretax Income	Income Tax Benefit	Net Income	Earnings per Share
First quarter	$ 137,701	$ 2,000	$ 139,701	$ 0.08
Second quarter	$ 180,022	$ 27,000	$ 207,022	$ 0.11
Third quarter	$ 159,011	$ 24,000	$ 183,011	$ 0.10

Note 11--REINSURANCE

The Company currently follows the general practice of reinsuring that portion of risk on the life of any individual which is in excess of $40,000 for individual policies (under yearly renewable term and coinsurance agreements) and $15,000 for group policies (under a group yearly renewable term agreement). Graded death benefit and simplified issue coverages above $4,000 are generally 50% reinsured, with the Life Insurance Subsidiaries maintaining a maximum $10,000 risk on any one policyholder. Individual and group accidental death coverage and a minor

portion of cancer coverage are 100% reinsured. To the extent that reinsuring companies are unable to meet obligations under reinsurance agreements, the Company would remain liable. Reinsurance premiums, expenses, recoveries and reserves related to reinsured business are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

Note 12--CONTINGENCIES

United Liberty, which the Company acquired in 1998, is defending an action in an Ohio state court brought by two policyholders. The Complaint refers to a particular class of life insurance policies that United Liberty issued over a period of years ending around 1971. It alleges that United Liberty's dividend payments on these policies from 1993 through 1999 were less than the required amount. It does not specify the amount of the alleged underpayment but implies a maximum of about $850,000. The plaintiffs also allege that United Liberty is liable to pay punitive damages, also in an unspecified amount, for breach of an implied covenant of good faith and fair dealing to the plaintiffs in relation to the dividends. The action has been certified as a class action on behalf of all policyholders who were Ohio residents and whose policies were still in force in 1993. United Liberty has denied the material allegations of the Complaint and is defending the action vigorously. Pre-trial discovery is continuing. United Liberty has filed a motion for summary judgment to which the plaintiffs have not yet responded. At United Liberty's request, an initial mediation session has been completed and negotiations are continuing. As a pre-requisite for the mediation, United Liberty offered to settle the matter for payments over time, which would include attorneys' fees, and which would be contingent upon an exchange or reformation of the insurance policies currently owned by the members of the class. At this stage of the litigation, the Company is unable to determine whether an unfavorable outcome of the action is likely to occur or, alternatively, whether the chance of such an outcome is remote. Therefore, at this time, management has no basis for estimating potential losses, if any. In addition, the Company is party to other lawsuits in the normal course of business. Management believes that recorded claims liabilities are adequate to ensure that these other suits will be resolved without material financial impact to the Company.

Note 13--FAIR VALUES OF FINANCIAL INSTRUMENTS

The fair values of financial instruments, and the methods used in estimating these values, are as follows:

Fixed Maturities: The fair values for fixed maturities are based on quoted market prices, where available. For those fixed maturities which are not actively traded, fair values are estimated using values obtained from independent pricing services. Available-for-sale fixed maturities are carried at fair value in the accompanying statements of financial condition. At December 31, 2002 and 2001, the fair value of available-for-sale fixed maturities was $103,953,815 and $77,534,516, respectively.

Equity Securities: The fair values for equity securities are based on quoted market prices. Equity securities are carried at fair value in the accompanying statements of financial condition. At December 31, 2002 and 2001, the fair value of equity securities was $7,761,892 and $8,116,958, respectively.

Short-Term Investments: The carrying amount of short-term investments approximates their fair value. At December 31, 2002 and 2001, the fair value of short-term investments was $632,381 and $652,192, respectively.

Cash and Cash Equivalents: The carrying amount of cash and cash equivalents approximates their fair value. At December 31, 2002 and 2001, the fair value of cash and cash equivalents was $6,699,171 and $18,433,626, respectively.

Mortgage Loans: The carrying amount of mortgage loans approximates their fair value. At December 31, 2001, the fair value of mortgage loans was $156,000. The Company held no mortgage loans at December 31, 2002.

Policy Loans: The carrying amount of policy loans approximates their fair value. At December 31, 2002 and 2001, the fair value of policy loans was $4,239,128 and $4,136,649, respectively.

Investment Contracts: The carrying amount of investment-type fixed annuity contracts approximates their fair value. At December 31, 2002 and 2001, the fair value of investment-type fixed annuity contracts was $9,805,082 and $9,907,941, respectively.

Notes Payable: The carrying amounts of notes payable approximate their fair values. At December 31, 2002 and 2001, the fair value of notes payable was $7,779,168 and $7,095,834, respectively.

Note 14--BENEFIT PLANS

The Company has a 401(k) savings plan for its full-time employees. The Company contributes matching contributions at the discretion of its Board of Directors. Company expense associated with this plan totaled $61,037, $57,532, and $46,353 in 2002, 2001 and 2000, respectively.

Note 15--RELATED PARTY TRANSACTIONS

The Company has various transactions with its President and Chairman of the Board (the "Chairman") or entities he controls. The Chairman provides investment portfolio management for the Company and its subsidiaries through SMC Advisors, Inc. (of which the Chairman is the principal officer, a director, and the sole shareholder). The investment portfolio management contracts provide for total annual fixed fees of $45,000 and incentive compensation equal to five percent (5%) of the sum of the net realized and unrealized capital gains in the fixed maturities and equity securities portfolios of the Company during each contract year. Any excess of net realized and unrealized capital losses over net realized and unrealized capital gains at the end of a contract year is not carried forward to the next contract year. Fixed fees totaled $45,000, $45,000, and $48,000 in 2002, 2001, and 2000, respectively. Incentive fees of $0, $48,168, and $207,369 were incurred and paid for 2002, 2001, and 2000, respectively. The Company also maintains a portion of its investments under a Trust Agreement with a bank controlled by the Chairman. Fees to the bank are based on assets held. Such fees were $100,675, $94,199, and $94,660 in 2002, 2001, and 2000, respectively. The Company also manages certain commercial real estate affiliated with its Chairman. The Company charges the real estate projects management and leasing fees at market rates, which totaled $213,070, $174,746, and $150,672 during 2002, 2001, and 2000, respectively. In December 2002, the Company borrowed $2,000,000 from its Chairman with interest payable quarterly at the greater of 6% per year or the commercial bank prime lending rate plus 1%.

Note 16 - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Effective January 1, 2001, the Company adopted Financial Accounting Standards Board Statement ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended by SFAS Nos. 137 and 138. This statement requires that all derivatives be recognized as either assets or liabilities in

the balance sheet at their fair value, and sets forth the manner in which gains or losses thereon are to be recorded. The treatment of such gains or losses is dependent upon the type of exposure, if any, for which the derivative is designated as a hedge. Currently, the Company has not designated any derivatives as hedges. Adoption of SFAS No. 133 resulted in a January 1, 2001 transition adjustment that reduced net income and increased accumulated other comprehensive income in 2001 by approximately $311,000. This adjustment consisted of a pretax total of $471,000 less a $160,000 tax benefit.

In June 2001, the Financial Accounting Standards Board issued Statements of Financial Accounting Standards No. 141, "Business Combinations", and No. 142, "Goodwill and Other Intangible Assets", effective for fiscal years beginning after December 15, 2001. Under the new rules, goodwill will no longer be amortized but is subject to annual impairment tests in accordance with the Statements. Other intangible assets will continue to be amortized over their useful lives. The Company applied the new rules on accounting for goodwill and other intangible assets beginning in the first quarter of 2002. Application of the nonamortization provisions of the Statement decreased the 2002 net loss approximately $96,000 ($0.06 per share). During 2002, the Company performed an impairment test of goodwill and concluded that no impairment adjustment was necessary.

Below is a proforma illustration of earnings adjusted to exclude goodwill amortization recorded during 2001 and 2000.

Year Ended December 31	2002	2001	
Net Income (Loss) excluding goodwill amortization	$ (2,572,060)	$ (6,109,562)	$
Goodwill amortization	---	96,013	
Net Income (Loss) - as reported	$ (2,572,060)	$ (6,205,575)	$
Net Income (Loss) per Share:			
Excluding goodwill amortization	$(1.50)	$(3.51)	
As reported	$(1.50)	$(3.57)	

Total goodwill outstanding at December 31, 2002 is $756,000 with $304,000 allocable to Broker Life, $270,000 to Home Service Life and $182,000 to Preneed Life.

Schedule I - Summary of Investments - Other than Investments in Relat
Citizens Financial Corporation and Subsidiaries
At December 31, 2002

	Cost or	Amount Which Sho

Type of Investment	Amortized Cost1	Fair Value	Balance She
Fixed maturity securities available-for-sale:			
US Government and government agencies and authorities	$ 39,440,068	$ 40,673,633	$ 40,673,6
Public utilities	2,467,257	2,525,312	2,525,3
Convertibles and bonds with warrants	1,878,614	1,529,287	1,529,2
All other corporate bonds	57,375,235	59,225,583	59,225,5
Total	101,161,174	103,953,815	103,953,8
Equity securities available-for-sale:			
Commons stocks:			
Banks, trusts and insurance companies	669,430	680,450	680,4
Industrial, miscellaneous and all other	3,075,630	3,118,040	3,118,0
Nonredeemable preferred stocks	3,363,675	3,963,402	3,963,4
Total	7,108,735	7,761,892	7,761,8
Investment real estate	3,252,424	3,252,424	3,252,4
Policy loans	4,239,128	4,239,128	4,239,1
Short-term investments	632,381	632,381	632,3
Total Investments	$ 116,393,842	$ 119,839,640	$ 119,839,6

1 Adjusted for declines in value believed to be other than temporary, totaling $1,569,399 for fixed maturity securities and $1,544,505 for equity securities and, as to fixed maturities, reduced by repayments and adjusted for amortization of premium and accrual of discounts.

Schedule II - Condensed Financial Information of Registrant
Citizens Financial Corporation
(Parent Company Only)
Condensed Balance Sheets

December 31	2002
Assets:	
Cash and cash equivalents	$ 1,166,107
Equity securities available-for-sale (cost of $1,531,555 and $1,275,702 in 2002 and 2001, respectively)	1,532,829
Fixed maturity securities available-for-sale (amortized cost of $101,750 in 2002 and $194,500 in 2001)	122,750
Investments in subsidiaries*	20,966,393
Furniture and equipment	1,296,421
Intercompany receivable*	634,435
Current and deferred federal income tax	255,546
Other assets	38,459
Total Assets	$ 26,012,940

Liabilities:	
Note payable to bank	$ 5,779,168
Note payable to related party	2,000,000
Current and deferred federal income tax	320,090
Net option positions	7,488
Other liabilities	148,562
Total Liabilities	8,255,308
Shareholders' Equity:	
Common stock	1,686,828
Additional paid-in capital	7,176,480
Accumulated other comprehensive income	14,701
Equity in accumulated other comprehensive income of subsidiaries*	2,209,058
Retained earnings	6,670,565
Total Shareholders' Equity	17,409,541
Total Liabilities and Shareholders' Equity	$ 26,012,940

Schedule II - Condensed Financial Information of Registrant
Citizens Financial Corporation
(Parent Company Only)
Condensed Statements of Operations

Year Ended December 31	2002	2001
Revenues:		
Net realized investment gains (losses)	$ (228,672)	$(1,953,848)
Service fees from subsidiaries	4,703,880	4,705,087
Interest and dividend income	49,234	206,940
Other income	28,280	38,816
Total Revenues	4,552,722	2,996,995
Expenses:		
Administrative and general expenses	4,784,744	4,743,159
Interest expense	305,715	532,962
Total Expenses	5,090,459	5,276,121
Income (loss) before income taxes and undistributed earnings of subsidiaries	(537,737)	(2,279,126)
Income tax expense (benefit)	(221,000)	(940,000)
Income (loss) before equity in undistributed	(316,737)	(1,339,126)

earnings of subsidiaries		
Equity in undistributed loss of subsidiaries	(2,255,323)	(4,866,449)
Net Income (Loss)	$(2,572,060)	$(6,205,575)

Schedule II - Condensed Financial Information of Registrant
Citizens Financial Corporation
(Parent Company Only)
Condensed Statements of Cash Flows

Year Ended December 31	2002	2001
Cash from operations	$ 1,032,505	$(1,423,335)
Cash flow from investing activities:		
Purchases of available-for-sale securities	(3,431,955)	(6,211,339)
Sales of available-for-sale securities	2,967,241	5,338,727
Redemption of subsidiary preferred stock*	---	---
Investment in subsidiaries*	(2,000,000)	(150,000)
Investment management fees	(9,623)	---
Additions to property and equipment, net	(30,279)	(40,392)
Change in investments, other	---	37,335
Net cash provided by (used in) investing activities	(2,504,616)	(1,025,669)
Cash flow from financing activities:		
Payments on notes payable - bank	(1,316,666)	(904,166)
Proceeds from note payable - affiliated party	2,000,000	---
Repurchase of capital stock	(139,445)	(396,450)
Net brokerage account loan repayment	---	---
Net cash provided by (used in) financing activities	543,889	(1,300,616)
Net increase (decrease) in cash and cash equivalents	(928,222)	(3,749,620)
Cash and cash equivalents at beginning of year	2,094,329	5,843,949
Cash and cash equivalents at end of year	$ 1,166,107	$ 2,094,329

Schedule III - Supplementary Insurance Information
Citizens Financial Corporation
For the Years Ended December 31, 2002, 2001, and 2000

Year Ended December 31 / Segment	Deferred Acquisition Costs	Policy and Claim Reserves	Unearned Premiums	Other Policy Claims and Benefits Payable	Premium Revenue	Net Investment and Other Income1	an
Column: A	B	C	D	E	F	G	
2002:							
Home Service Life	$3,717,940	$ 33,468,638	$ ---	$ 502,085	$ 7,334,030	$1,926,067	$
Broker Life	3,621,843	44,407,746	2,998	643,845	3,621,053	2,343,036	
Preneed Life	2,414,288	38,792,405	---	178,798	17,993,645	1,712,491	1
Dental	---	296,369	5,384	222,496	8,182,483	26,774	
Other Health	161,217	1,705,655	239,243	249,971	1,347,939	84,668	
Total	$9,915,288	$118,670,813	$247,625	$1,797,195	$38,479,150	$6,093,036	$3
2001:							
Home Service Life	$3,297,247	$ 32,093,694	$ ---	$ 516,265	$ 7,152,242	$2,137,878	$
Broker Life	3,451,936	44,067,779	3,147	344,048	3,812,841	2,684,445	
Preneed Life	1,665,278	27,239,439	---	273,207	8,397,911	1,576,494	
Dental	---	264,235	5,540	295,344	7,988,620	36,754	
Other Health	164,962	1,590,144	244,043	302,892	1,392,762	94,801	
Total	$8,579,423	$105,255,291	$252,730	$1,731,756	$28,744,376	$6,530,372	$2
2000:							
Home Service Life	$2,739,204	$ 30,865,491	$ ---	$ 678,066	$ 6,906,473	$2,129,532	$
Broker Life	3,184,922	44,046,164	3,577	581,758	3,664,072	2,664,812	
Preneed Life	425,320	22,902,433	---	192,397	3,982,948	1,362,982	
Dental	---	303,550	7,680	298,881	7,892,356	41,242	
Other Health	162,502	1,667,389	206,413	269,445	1,376,575	92,741	
Total	$6,511,948	$ 99,785,027	$217,670	$2,020,547	$23,822,424	$6,291,309	$1

Schedule IV - Reinsurance
Citizens Financial Corporation
For the Years Ended December 31, 2002, 2001, and 2000

Year Ended December 31	Gross Amount	Ceded to To Other Companies	Assumed From Other Companies	
2002:				

Life insurance in force:	$792,722,000	$ 96,202,000	$6,199,775	$702
Premiums:				
Life insurance	$ 29,977,144	$ 1,010,513	$ 21,896	$ 28
Accident & health insurance	9,723,549	232,926	---	9
Total	$ 39,700,693	$ 1,243,439	$ 21,896	$ 38

2001:

Life insurance in force:	$812,515,000	$109,227,000	$6,768,604	$710
Premiums:				
Life insurance	$ 20,387,653	$ 1,051,574	$ 26,915	$ 19
Accident & health insurance	9,555,188	173,806	---	9
Total	$ 29,942,841	$ 1,225,380	$ 26,915	$ 28

2000:

Life insurance in force:	$799,576,000	$100,829,000	$7,297,000	$706
Premiums:				
Life insurance	$ 15,458,588	$ 940,202	$ 35,107	$ 14
Accident & health insurance	9,341,114	72,183	---	9
Total	$ 24,799,702	$ 1,012,385	$ 35,107	$ 23

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

There has been no change in accountants nor have there been any disagreements on accounting and financial disclosure requiring disclosure pursuant to the Instructions to this Item.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

The information required by this Item is set forth under the captions: "Election of Directors", "Executive Officers", and "Section 16(a) Beneficial Ownership Reporting Compliance" in the Board of Director's Proxy Statement for the Annual Meeting of Shareholders of the Company now scheduled for May 22, 2003, and such information is here incorporated by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this Item is set forth under the captions: "Executive Compensation", "Board of Directors Report on Executive Compensation", "Performance Graph" and "Compensation Committee Interlocks and Insider Participation" of the Board of Directors' Proxy Statement for the Annual Meeting of Shareholders of the Company now scheduled for May 22, 2003, and such information is here incorporated by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this Item is set forth under the caption: "Security Ownership of Certain Beneficial Owners and Management" in the Board of Directors' Proxy Statement for the Annual Meeting of Shareholders of the Company now scheduled for May 22, 2003, and such information is here incorporated by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information required by this Item is set forth under the caption: "Certain Transactions Involving Directors and Executive Officers" in the Board of Directors' Proxy Statement for the Annual Meeting of Shareholders of the Company now scheduled for May 22, 2003, and such information is here incorporated by reference.

ITEM 14. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES. Based on an evaluation of the Company's disclosure controls and procedures within the past 90 days, Company officers have concluded that such controls and procedures provide reasonable assurance that material information relating to the Company, including its consolidated subsidiaries, is made known to the Company's principal executive and financial officers.

CHANGES IN INTERNAL CONTROLS. There have been no significant changes in the Company's internal controls or changes in other factors that could significantly affect these controls subsequent to their evaluation, nor has the Company implemented any corrective actions regarding significant deficiencies or material weaknesses in internal controls.

It should be noted that any system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system are met. In addition, the design of any control system is based in part upon certain assumptions about the likelihood of future events. Because of these and other inherent limitations of control systems, there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

The following documents are filed as part of this Form 10-K:

(a) Financial Statements and Financial Statement Schedules.

The audited Consolidated Financial Statements of the Company and its subsidiaries, the Financial Statements Schedules (including: Schedule I - Summary of Investments - Other than Investments In Related Parties, Schedule II - Condensed Financial Information of Registrant, Schedule III - Supplementary Insurance Information, and Schedule IV - Reinsurance), and the related Report of Independent Auditors listed in the Index to Financial Statements and Financial Statement Schedules appearing under Item 8 of this Form 10-K.

(b) Reports on Form 8-K.
December 19, 2002 - Item 5. Other Events. The Company disclosed borrowing $2,000,000 from its Chairman and authorization of an additional $250,000 of common stock repurchase capacity.

(c) Exhibits.
The exhibits listed in the Index to Exhibits appearing on page 58.

Pursuant to paragraph (b)(4)(iii) of Item 601 of Regulation S-K, the Company agrees to furnish to the Commission upon request copies of instruments defining the rights of holders of the Company's long term debt.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CITIZENS FINANCIAL CORPORATION

April 7, 2003 By: /s/ Darrell R. Wells

Darrell R. Wells
President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

/s/ Darrell R. Wells Darrell R. Wells	Director and President (principal executive officer)	April 7, 2003
/s/ Lane A. Hersman Lane A. Hersman	Director and Executive Vice President	April 7, 2003
/s/ Brent L. Nemec Brent L. Nemec	Vice President, Accounting, Chief Financial Officer, and Treasurer (principal financial and accounting officer)	April 7, 2003
/s/ John H. Harralson, Jr. John H. Harralson, Jr.	Director	April 7, 2003

/s/ Frank T. Kiley --- Frank T. Kiley	Director	April 7, 2003
/s/ Earle V. Powell --- Earle V. Powell	Director	April 7, 2003
/s/ Thomas G Ward --- Thomas G. Ward	Director	April 7, 2003
/s/ Margaret A. Wells --- Margaret A. Wells	Director	April 7, 2003

Certification of Principal Executive Officer
Certification for Annual Report on Form 10K

I, Darrell R. Wells, certify that:

1) I have reviewed this annual report on Form 10-K of Citizens Financial Corporation;

2) Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3) Based on my knowledge, the financial statements and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

   c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit

committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6) The registrant's other certifying officer and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Signature and Title: /s/ Darrell R. Wells Date: 4/7/2003
President and Chief Executive Officer

Certification of Principal Financial Officer
Certification for Annual Report on Form 10K

I, Brent L. Nemec, certify that:

1) I have reviewed this annual report on Form 10-K of Citizens Financial Corporation;

2) Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3) Based on my knowledge, the financial statements and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4) The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual (the "Evaluation Date"); and

c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5) The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6) The registrant's other certifying officer and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Signature and Title: /s/ Brent L. Nemec — Date: 4/7/2003
Vice President and
Chief Financial Officer

INDEX TO EXHIBITS
(Item 15(c))

The documents listed in the following table are filed as Exhibits in response to Item 15(c). Exhibits listed that are not filed herewith are incorporated herein by reference.

Exhibit No.	Description
3.1	Restated Articles of Incorporation of the Company dated August 12, 1996 (filed as Exhibit 3.1 to the Company's Form 10-KSB dated March 31, 1999)
3.2	Bylaws of the Company adopted September 12, 1990 as amended March 25, 1994 (filed as Exhibit 3.2 to the Company's Form 10-K dated March 28, 1996)
4	Provisions of Articles of Incorporation of the Company Defining the Rights of Holders of Class A Stock (filed as Exhibit 4 to the

Company's Form 10 Registration Statement)

10.1 Investment Management Agreements dated July 1,1994 between Citizens Security and the Company and SMC Advisors, Inc. (filed as Exhibit 10.1 to the Company's Form 10-K dated March 29, 1995)

10.1B Investment Management Agreement dated June 1, 1998 between United Liberty and SMC Advisors, Inc. (filed as Exhibit 10.1B to the Company's Form 10-KSB dated March 31, 1999)

10.1C Investment Management Agreement dated February 6, 2000 between Citizens Insurance and SMC Advisors, Inc. (filed as Exhibit 10.1C to the Company's Form 10-KSB dated March 29, 2000)

10.9 Form of Employment Agreement with Certain Executives of the Company and Schedule of Data (filed as Exhibit 10.9 to the Company's Form10-K dated March 28, 1996)*

10.10 1999 Stock Option Plan (filed as exhibit to the Company's proxy statement for annual meeting of shareholders held on May 20, 1999)*

10.11 2002 Promissory Note to Darrrell R. Wells and related Subordination Agreement (filed herewith)

10.12 Executive Severance Plan* (filed herewith)

21.2 Subsidiaries of the registrant (filed as Exhibit 21.2 to the Company's Form 10-K dated March 30, 2002)

23.3 Consent of Independent Auditors (filed herewith)

99.1 Section 906 - Chief Executive Officer Certification (filed herewith)

99.2 Section 906 - Chief Financial Officer Certification (filed herewith)

* Management contract or compensatory plan or arrangement.