American Life & Security Corp.

Statutory Financial Statements and
Supplemental Schedules
December 31, 2013 and 2012
(With Independent Auditors' Report Thereon)

McGladrey

Assurance ▪ Tax ▪ Consulting

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Independent Auditor's Report

The Board of Directors
American Life & Security Corp.

Report on the Financial Statements

We have audited the accompanying statutory financial statements of American Life & Security Corp. (the Company), which comprise the statutory statements of admitted assets, liabilities, and capital stock and surplus of American Life & Security Corp. as of December 31, 2013 and 2012, and the related statutory statements of operations, capital stock and surplus, and cash flows for the years then ended and the related notes to the statutory financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these statutory financial statements in accordance with the accounting practices prescribed or permitted by the Insurance Department of the State of Arizona; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of statutory financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these statutory financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the statutory financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the statutory financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the statutory financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the statutory financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the statutory financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 2 to the statutory financial statements, American Life & Security Corp. prepared these financial statements using accounting practices prescribed or permitted by the Insurance Department of the State of Arizona, which is a basis of accounting other than accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between these statutory accounting practices and accounting principles generally accepted in the United States of America are material and are described in Note 2.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the "Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles" paragraph, the financial statements referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of American Life & Security Corp. and its subsidiaries as of December 31, 2013 and 2012, or the results of its operations or its cash flows thereof for the years then ended.

Opinion on Regulatory Basis of Accounting

In our opinion, the statutory financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, and capital and surplus of American Life & Security Corp.as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years then ended, on the basis of accounting described in Note 2.

Report on Supplemental Schedules

Our audits were conducted for the purpose of forming an opinion on the basic statutory financial statements taken as a whole. The accompanying Supplemental Summary Investment Schedule as of December 31, 2013 and Supplemental Investment Risks Interrogatories and Selected Financial Data as of December 31, 2013 and for the year then ended (Supplemental Schedules) are presented for purposes of additional analysis and are not a required part of the basic statutory financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the statutory financial statements. The effects on the Supplemental Schedules of the variances between the statutory accounting practices and accounting principles generally accepted in the United States of America are material and are described in Note 2. As a consequence, the Supplemental Schedules do not present fairly, in conformity with accounting principles generally accepted in the United States of America, such information of the Company as of December 31, 2013 and for the year then ended. The Supplemental Schedules have been subjected to the auditing procedures applied in the audit of the statutory financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the statutory financial statements or to the statutory financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the Supplemental Schedules are fairly stated in all material respects in relation to the statutory financial statements taken as a whole.

McGladrey LLP

Omaha, Nebraska
June 26, 2014

American Life & Security Corp.

Statutory Statements of Admitted Assets, Liabilities, and Capital Stock and Surplus
December 31, 2013 and 2012

Admitted Assets	**2013**	2012
Cash and invested assets:		
Bonds	**$ 10,251,174**	$ 8,400,541
Preferred stock	**75,000**	75,000
Common stock of affiliates	**1,640,639**	1,588,775
Common stock of nonaffiliates	**-**	103,652
Mortgage loans on real estate	**642,327**	647,139
Properties held for the production of income	**553,849**	565,889
Policy loans	**368,404**	274,664
Cash	**596,504**	914,345
Total cash and invested assets	**14,127,897**	12,570,005
Interest and dividends due and accrued	**118,274**	122,938
Premiums and considerations	**170,831**	226,664
Equipment, net of accumulated depreciation of $192,610 and $126,725, respectively	**108,578**	111,072
Receivable from parent company	**147,197**	33,761
Other assets	**108,966**	12,572
Total admitted assets	**$ 14,781,743**	$ 13,077,012
Liabilities and Capital Stock and Surplus		
Liabilities:		
Reserve for life contracts	**$ 11,950,140**	$ 9,759,226
Reserve for accident and health contracts	**18,361**	18,225
Liability for deposit-type contracts	**369,915**	455,236
Contract claims	**178,233**	138,925
Accrued expenses and taxes	**44,312**	275,920
Amounts payable on reinsurance assumed	**25,202**	113,696
Advance premiums and amounts held or due agents	**13,739**	8,250
Interest maintenance reserve	**197,641**	211,156
Remittances and items not allocated	**42,669**	45,357
Asset valuation reserve	**76,331**	69,408
Total liabilities	**12,916,543**	11,095,399
Capital stock and surplus		
Surplus notes	**550,000**	550,000
Capital stock:		
Common stock, $420 par value. 10,000 shares authorized; issued and outstanding 2,500 shares as of December 31, 2013 and 2012	**1,050,000**	1,050,000
Gross paid-in and contributed surplus	**9,975,221**	9,975,221
Total capital stock	**11,025,221**	11,025,221
Unassigned deficit	**(9,710,021)**	(9,593,608)
Total capital stock and surplus	**1,865,200**	1,981,613
Total liabilities and capital stock and surplus	**$ 14,781,743**	$ 13,077,012

See Notes to Statutory Financial Statements.

American Life & Security Corp.

Statutory Statements of Operations
Years Ended December 31, 2013 and 2012

	2013	2012
Income:		
Premiums earned	$ 4,642,004	$ 4,764,505
Investment income earned, net of investment expenses of $32,066 and $24,163, respectively	420,118	426,869
Amortization of interest maintenance reserve	32,575	22,417
Miscellaneous income	7,382	14,072
Total income	5,102,079	5,227,863
Benefits and expenses:		
Increase in aggregate reserves for life contracts	2,190,914	1,453,972
Benefits to policyholders	926,914	1,250,327
Interest and adjustments on deposit-type contract funds	7,517	12,480
Commissions	539,499	1,111,244
Taxes, licenses and fees	199,974	191,739
General expenses	1,266,880	2,117,536
Total benefit and expenses	5,131,698	6,137,298
Net loss from operations before income taxes and net realized investment gain (loss)	(29,619)	(909,435)
Income taxes	-	-
Net loss from operations after income taxes and before net realized investment gain (loss)	(29,619)	(909,435)
Net realized gain (loss) on investments, excluding amounts transferred to IMR of $19,060 and $171,283, respectively	9,122	(1,614)
Net loss	$ (20,497)	$ (911,049)

See Notes to Statutory Financial Statements.

American Life & Security Corp.

Statutory Statements of Capital Stock and Surplus
Years Ended December 31, 2013 and 2012

	2013	2012
Capital stock:		
Balance at beginning of year	**$ 1,050,000**	$ 1,050,000
Transfer to surplus	**-**	-
Balance at end of year	**1,050,000**	1,050,000
Surplus notes:		
Balance at beginning of year	**550,000**	950,000
Payments	**-**	(400,000)
Balance at end of year	**550,000**	550,000
Gross paid-in and contributed surplus:		
Balance at beginning of year	**9,975,221**	9,975,221
Paid in surplus	**-**	-
Balance at end of year	**9,975,221**	9,975,221
Unassigned surplus:		
Balance at beginning of year	**(9,593,608)**	(8,204,240)
Net loss	**(20,497)**	(911,049)
Change in unrealized capital losses	**(104,253)**	32,190
Change in nonadmitted assets	**34,965**	(468,991)
Change in deferred taxes	**-**	-
Change in asset valuation reserve	**(6,923)**	(13,999)
Amortization of goodwill	**(27,518)**	(27,519)
Other	**7,813**	-
Balance at end of year	**(9,710,021)**	(9,593,608)
Total capital stock and surplus	**$ 1,865,200**	$ 1,981,613

See Notes to Statutory Financial Statements.

American Life & Security Corp.

Statutory Statements of Cash Flows
Years Ended December 31, 2013 and 2012

	2013	2012
Cash from operations:		
Premiums collected, net	**$ 4,674,482**	$ 4,716,801
Benefit and loss related payments	**(983,481)**	(1,231,899)
Underwriting expenses paid	**(2,176,484)**	(3,432,913)
Investment income, net	**417,193**	479,879
Miscellaneous income	**7,382**	14,072
Net cash provided by operations	**1,939,092**	545,940
Cash from investments:		
Proceeds from bonds sold or matured	**9,623,979**	11,503,693
Proceeds from stocks sold	**170,751**	159,120
Proceeds from mortgage loans repaid	**11,442**	6,430
Miscellaneous proceeds	**12,040**	-
Cost of bonds acquired	**(11,529,442)**	(11,531,914)
Cost of stocks acquired	**(265,783)**	(47,527)
Net change in contract loans	**-**	50,474
Net cash (used in) provided by investments	**(1,977,013)**	140,276
Cash provided by financing and miscellaneous sources:		
Payments on surplus notes	**-**	(400,000)
Net (withdrawals) deposits on deposit type contracts	**(85,321)**	61,193
Other cash (uses)	**(194,599)**	(82,570)
Net cash used in financing and miscellaneous sources	**(279,920)**	(421,377)
Net (decrease) increase in cash	**(317,841)**	264,839
Cash at beginning of year	**914,345**	649,506
Cash at end of year	**$ 596,504**	$ 914,345

See Notes to Statutory Financial Statements.

Note 1. Company Overview

American Life & Security Corp. (American Life or the Company) is a wholly-owned subsidiary of Midwest Holding Inc. (MHI). The Company is the surviving entity of the August 2011 merger of Old Reliance Insurance Company (Old Reliance) and American Life & Security Corp. Old Reliance was a Life and Accident and Health Insurance Company organized in 1960 under the laws of the State of Arizona.

Immediately following the purchase, MHI merged American Life into Old Reliance and renamed the new entity American Life & Security Corp. As a result of the transaction, American Life was domiciled in the state of Arizona. The Company is licensed in fourteen states and engaged in the business of underwriting, selling, and servicing life insurance and annuity policies.

The Company owns 100% of the common stock of Capital Reserve Life Insurance Company (Capital Reserve). Capital Reserve is a stock life insurance company domiciled in Missouri and is authorized to write business in Missouri and Kansas. The Company purchased Capital Reserve on June 20, 2010 for $1,956,433.

Note 2. Summary of Significant Accounting Policies

<u>Basis of presentation</u>: The accompanying statutory financial statements of the Company have been prepared in conformity with accounting practices prescribed or permitted by the Arizona Department of Insurance, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Prescribed statutory accounting policies include a variety of publications of the National Association of Insurance Commissioners (NAIC), as well as state laws, regulations, and general administrative rules. Permitted statutory accounting practices encompass all accounting policies other than those prescribed. The NAIC Accounting Practices and Procedures Manual (NAIC SAP) has been adopted as a component of prescribed practices by the State of Arizona. The Company does not employ any practices not prescribed by the NAIC or the Arizona Department of Insurance in the preparation of its statutory financial statements. Certain immaterial reclassifications have been made to the prior period results to conform with the current period's presentation with no impact on results of operations or capital and surplus.

The more significant differences between statutory accounting practices and GAAP are as follows:

- Investments in bonds with an NAIC rating of 1 through 5 are carried at amortized cost; whereas bonds with an NAIC rating of 6 are written down to the lower of amortized cost or fair value by charging statutory surplus. Under GAAP, bonds are classified into three categories: held to maturity, available for sale, or trading. Bonds held to maturity are stated at amortized cost; bonds available for sale are stated at fair value and the resulting unrealized gains or losses, net of applicable income taxes, are charged or credited to capital and surplus; and bonds held for trading are reported at fair value and the resulting unrealized gains and losses are reported in earnings, net of related taxes.

  The fair value of investments on a statutory basis is determined by the SVO, where as for GAAP, the fair value of investments is determined based on the expected exit price.

- Assets having economic value other than those that can be used to fulfill policyholder obligations are categorized as "nonadmitted assets" and are not permitted to be included in the statutory financial statements of admitted assets, liabilities, and capital and surplus, whereas, for GAAP, these assets are recognized in the balance sheet. Included with nonadmitted assets are furniture, equipment and supplies, prepaid expenses, receivables over 90 days outstanding, certain deferred tax assets and other items that do not meet statutory criteria for admitted assets.

Note 2. Summary of Significant Accounting Policies (Continued)

- Deferred federal income taxes are provided for the tax effects of certain income and expense items recognized for income tax purposes in different years than for financial reporting purposes. The change in the deferred tax asset or liability is reflected in capital and surplus. GAAP requires the change to be reported in earnings. Admittance testing may result in a charge to capital and surplus for nonadmitted portions of the deferred tax asset. State taxes are not considered for statutory purposes in calculating a deferred tax asset or liability, however, they are considered for GAAP purposes.

  Both statutory and GAAP guidance requires a valuation allowance be established where the deferred tax asset is reduced, if based on the weight of available evidence it is more likely than not that some portion or all of a gross deferred tax asset will not be realized, to its realizable value. Changes in valuation allowance are reported in a similar manner to which changes in deferred tax assets and liabilities are reported, as noted above.

- The statutory financial statements are presented net of the effects of reinsurance, whereas, for GAAP, the financial statements are presented gross of the effects of reinsurance.

- Deferred and uncollected premiums represent premiums receivable in installments (semiannually, quarterly, and monthly) not yet due or collected, but for which policy reserves based on full annual premiums have been provided. Such premiums are reported net of loading expenses, whereas for GAAP, such balances are reported gross.

- Benefits for universal life policies and annuity contracts consist of premiums received as opposed to GAAP, which records policy and contract fees charged for the cost of insurance, policy administrative charges, amortization of policy initiation fees, and surrender contract charges as revenues.

- Premium receipts and benefits on universal life policies and annuities are recorded as revenue and expense for statutory purposes. Under GAAP, revenues on universal life policies comprised of contract charges and fees, which are recognized when assessed against the policyholder's account balance. Additionally, under GAAP, premium receipts on universal life policies and annuities are considered deposits and are recorded as interest-bearing liabilities.

- Capital contributions can be made after the reporting period and, with approval from the Arizona Commissioner of Insurance, can be classified as capital contributions for a prior reporting period for statutory purposes. Under GAAP, these capital contributions are recorded as capital contributions on the date they are made.

- Acquisition costs, such as commissions and other costs incurred in connection with acquiring new business, are charged to current operations as incurred, whereas premiums are taken into income over the premium-paying period of the policies. Under GAAP, to the extent recoverable, acquisition costs are capitalized and charged to operations as the revenues are recognized or future profits emerge.

- Commissions allowed by reinsurers on business ceded are reported as income when received rather than being deferred and, to the extent recoverable, amortized with deferred policy acquisition costs, as required under GAAP.

- Comprehensive income is not determined for statutory reporting purposes, whereas, for GAAP, such income is presented.

Note 2. Summary of Significant Accounting Policies (Continued)

- The statutory statement of cash flows differs in certain respects from the presentation required within GAAP literature, including the presentation of changes in cash and short-term investments instead of cash and cash equivalents. Short-term investments include securities with original maturities of one year or less. For GAAP, cash equivalents include highly liquid investments with a maturity of three months or less at acquisition. Further, GAAP requires the presentation of a reconciliation of net income to cash provided by operating activities.

- The statutory financial statements are prepared in a form using language and groupings substantially the same as the annual statements of the Company filed with the NAIC and the state regulatory authorities, which differ from the presentation and disclosures of financial statements presented under GAAP reporting.

- The accounts of wholly owned subsidiaries are not consolidated with those of the Company as would be required under GAAP but are recorded at the equity of statutory basis net assets. Under STAT, goodwill created from a statutory merger is limited in the aggregate to 10% of the acquiring entity's statutory capital and surplus. Goodwill is amortized to unrealized gains and losses over a period not to exceed 10 years. Under GAAP, goodwill is not subject to any such limitation and there is no amortization of goodwill. Under both STAT and GAAP, goodwill is subject to periodic impairment evaluation.

- The Company is required to establish an asset valuation reserve (AVR) and an interest maintenance reserve (IMR). The AVR provides for a standardized statutory investment valuation reserve for bonds, common stocks, mortgage loans, short-term investments, and other invested assets. Changes in this reserve are recorded as charges or credits to capital and surplus. The IMR is designed to defer net realized capital gains and losses resulting from changes in interest rates in the market and to amortize them into income over the remaining life of the bond or mortgage loan sold. The IMR represents the unamortized portion not yet taken into income. AVR and IMR are not recorded for GAAP.

- The statutory financial statements present surplus notes as a component of capital stock and surplus, whereas, for GAAP, the financial statements present surplus notes as a liability.

Note 2. Summary of Significant Accounting Policies (Continued)

A reconciliation of net income and capital and surplus, as presented in the accompanying statutory financial statements, and GAAP as of and for the years ended December 31, 2013 and 2012 is as follows:

	Net Loss		Capital and Surplus	
	2013	2012	**2013**	2012
Amounts stated in conformity with NAIC SAP	**$ (20,497)**	$ (911,049)	**$ 1,865,200**	$ 1,981,613
Gains on sales of investments, net of IMR amortization	**34,142**	148,866	**197,641**	211,156
Asset valuation reserve	**-**	-	**76,331**	69,408
Investments	**(615,490)**	123,077	**(510,470)**	767
DAC	**(78,722)**	494,897	**2,524,570**	2,603,292
Nonadmitted assets	**-**	-	**117,485**	152,450
Surplus notes	**-**	-	**(550,000)**	(550,000)
VOBA	**(142,786)**	(163,976)	**821,771**	964,557
Intangible assets	**-**	-	**700,000**	700,000
Goodwill	**-**	-	**1,129,824**	1,129,824
Property and equipment	**(52,253)**	(52,254)	**147,252**	199,505
Carrying value of reserves	**(77,218)**	(422,732)	**(2,231,439)**	(2,154,221)
Miscellaneous	**437,254**	312,288	**(27,657)**	(134,956)
Amounts stated in conformity with GAAP	**$ (515,570)**	$ (470,883)	$ 4,260,508	$ 5,173,395

Risk and uncertainties: Certain risks and uncertainties are inherent in the Company's day-to-day operations and in the process of preparing its statutory financial statements. The more significant of those risks and uncertainties, as well as the Company's method for mitigating the risks, are presented below and throughout the notes to the statutory financial statements.

- *Use of Estimates* – The preparation of statutory financial statements requires management to make estimates and assumptions that affect the reported amounts of admitted assets and liabilities and disclosure of contingent assets and liabilities at the date of the statutory financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

- *Reinsurance* – Reinsurance contracts do not relieve the Company from its obligations to insureds. Failure of reinsurers to honor their obligations could result in losses to the Company. The Company evaluates the financial condition of its reinsurers to minimize its exposure to losses from reinsurer insolvencies. Management believes that any liability arising from this contingency would not be material to the Company's financial position.

- *Investments* – The Company is exposed to risks that issuers of securities owned by the Company will default or that interest rates will change and cause a decrease in the market value of its investments.

Note 2. Summary of Significant Accounting Policies (Continued)

- *Loss Reserves* – The reserves for policy and contract claims consist of case-basis estimates for reported claims and estimates for unreported claims based on past claims-reporting experience. The management of the Company believes reserves for policy and contract claims are adequate to cover the ultimate liability. However, the ultimate claim costs may vary from the amounts presently provided.

- *External Factors* – The Company is highly regulated by the state in which it is domiciled. Such regulations, among other things, may limit the amount of rate increases on policies and impose restrictions on the amount and type of investments made and the minimum surplus required to conduct business in the state. The impact of regulatory initiatives in response to the recent financial crisis, including the Dodd-Frank Wall Street Reform and Consumer Protection Act, could subject the Company to substantial additional regulation.

- *Risk-Based Capital* – The NAIC has developed life risk-based capital (RBC) standards that relate an insurer's reported statutory surplus to the risks inherent in its overall operations. The RBC formula uses the statutory annual statement to calculate the minimum indicated surplus level to protect the Company from various risks that it faces. The NAIC model law calls for various levels of regulatory action based on the magnitude of an indicated RBC capital deficiency, if any. The Company continues to monitor its internal requirements and the NAIC's RBC requirements. The Company has determined that its surplus levels are in excess of the minimum capital requirements for all RBC action levels. Management believes that the Company's surplus levels are sufficient to support the level of risk inherent in its operations.

The credit quality of the bond portfolio at December 31, 2013 and 2012 is presented in the following table:

	2013		2012	
	Amortized Cost	**Percentage**	Amortized Cost	Percentage
Class 1 - highest quality	**$ 8,467,566**	**83%**	$ 4,646,684	55%
Class 2 - high quality	**1,783,608**	**17%**	3,753,857	45%
Class 3 - medium quality	**-**	**0%**	-	0%
Class 4 - low quality	**-**	**0%**	-	0%
Class 5 - lower quality	**-**	**0%**	-	0%
Class 6 - in or near default	**-**	**0%**	-	0%
	$ 10,251,174	**100%**	$ 8,400,541	100%

Bonds with ratings from AAA to BBB as assigned by Standard & Poor's Corporation are generally considered as investment grade securities. Some securities issued by the U.S. government or an agency thereof are not rated but are considered to be investment grade. The NAIC regards U.S. Treasuries and agencies and all A ratings as Class 1 (highest quality), BBB ratings as Class 2 (high quality), BB ratings as Class 3 (medium quality), B ratings as Class 4 (low quality), C ratings as Class 5 (lower quality), and D ratings as Class 6 (in or near default).

Note 2. Summary of Significant Accounting Policies (Continued)

Investments: Investments are valued as prescribed by the NAIC and are generally reported as follows:

- Bonds and redeemable preferred stocks assigned an NAIC rating of 1 to 5 are recorded at amortized cost using the scientific method (constant yield method) with bonds containing a call provision being amortized to the call or maturity date, whichever results in a lower asset value. Bonds and redeemable preferred stocks assigned a rating by NAIC of 6 are adjusted to the lower of amortized cost or fair value as published by the NAIC, with the offset reported as a change in capital and surplus.

- Redeemable preferred stocks are stated at the lower amortized cost or NAIC fair values. Perpetual preferred stocks are carried at NAIC fair value.

- Unaffiliated common stocks are carried at fair value. The change in the stated value is recorded as a change in net unrealized gains (losses), a component of unassigned surplus, net of applicable taxes or as a realized loss through operations if considered to be other-than-temporarily impaired.

- Mortgage loans are carried at the aggregate unpaid principal balance. The portion of loans in excess of 80% of the loan to value ratio are nonadmitted. Management believes that the Company's historic collection experience supports this practice.

- Properties held for the production of income is comprised of ten condominiums in Hawaii. The Company provides for depreciation of properties held for the production of income using the straight-line method over 50 years which is the estimated useful life of the assets. Expenditures resulting in significant betterment or improvement to a property are included in the cost of the property. Repairs and renewals of a minor nature are charged to operations as incurred. Depreciation expense was $12,040 and $12,121, for the years ended December 31, 2013 and 2012, respectively.

- Policy loans are recorded at the aggregate unpaid balances and are collateralized by the cash surrender value of the policyholder's underlying life insurance policy.

- Stocks of insurance affiliates in which the Company has an interest of 10% or more are recorded based on the underlying audited statutory equity of the respective entities' financial statements. The change in the stated value is recorded as a change in net unrealized capital gains (losses), a component of unassigned surplus.

The assessment of other-than-temporary impairments is performed on a case-by-case basis. Factors considered by management in determining whether an other-than-temporary impairment exists (in other than loan-backed or structured investment securities) include: the financial condition, business prospects and creditworthiness of the issuer, the length of time and extent to which fair value has been less than cost for equity securities or amortized cost for fixed income securities, and the Company's intent and ability to retain such investments until the fair value recovers. If it is determined that the decline in fair market value is other than temporary, the carrying amount of the investment is written down to fair value as its new basis and the amount of the write-down is recorded as a realized loss.

Investment income consists primarily of interest and dividends. Interest is recognized on the accrual basis and dividends are recorded as earned at the ex-dividend date for stocks other than mandatorily redeemable, preferred stocks which are accrued to the redemption price.

Note 2. Summary of Significant Accounting Policies (Continued)

Dividends or distributions received from affiliates are recognized in investment income when declared to the extent that they are not in excess of the undistributed accumulated earnings attributable to the investee. Dividends or distributions declared in excess of the undistributed accumulated earnings attributable to the investee shall reduce the carrying amount of the investment.

Investment income due and accrued 90 days past due is nonadmitted. There was no investment income due and accrued excluded from capital and surplus at December 31, 2013 and 2012.

Realized gains and losses on securities transactions are determined on a specific identification basis and are included in the statutory statements of operations, net of federal income tax, subject to the provisions of the interest maintenance reserve.

The Company may, from time to time, sell invested assets subsequent to the financial statement date that were considered temporarily impaired at the financial statement date for several reasons. For all subsequent sales of invested assets that were considered temporarily impaired at the financial statement date, the Company contemporaneously documents its rationale for its change in intent or ability to hold to recovery. The rationale for the change in the Company’s ability or intent generally focuses on changes in the economic facts and circumstances related to the invested asset subsequent to the financial statement date, significant unforeseen changes in the Company’s liquidity needs, or changes in tax laws or the regulatory environment.

Cash and short-term investments: Cash and short-term investments consist of cash on deposit with financial institutions and investments with original maturities of less than one year at the date of acquisition. These investments are carried at cost, which approximates fair value. At December 31, 2013 and 2012, the Company had substantially all of its cash on deposit with a bank and had not short-term investments. The Company has cash on deposit with financial institutions which at times may exceed the Federal Deposit Insurance Corporation limits. The Company has not suffered any losses in the past and does not believe it is exposed to any significant credit risk in these balances.

Revenue recognition and related expenses: Life premiums are recognized as income over the premium-paying period of the related policies. Premium income includes reinsurance assumed and is reduced by premiums ceded. Increases in policy benefit reserves, policy acquisition costs, and other period expenses are charged to operations as incurred. Reinsurance commissions, administration, and expense allowances are recognized when incurred in accordance with the contract terms.

Reserves: Policy reserves for traditional and flexible premium insurance are computed principally by using the commissioners' reserve valuation method (CRVM) or the net level premium method with assumed interest rates and mortality as prescribed by regulatory authorities. Tabular interest, tabular less actual reserves released, and tabular cost for all life contracts are determined based upon statutory regulations.

The Company's deposit-type contracts are supplemental contracts, dividends, and premiums on deposit and are reported as policyholder funds left on deposit. Premiums on deposit relate to life products. Interest on deposit-type funds is compounded annually.

Policy reserves for life insurance include claim reserves and unearned premiums. Claims reserves, including incurred but not reported claims, represent management's estimate of the ultimate liability associated with unpaid policy claims, based upon analysis of past experience. To the extent that the ultimate liability differs from the amounts recorded, such differences are reflected in operations when additional information becomes known.

Note 2. Summary of Significant Accounting Policies (Continued)

The Company records a premium deficiency reserve when it is established that future premium and current reserves are not sufficient to cover future claim payments and expenses on individual insurance programs. The Company currently does not have a premium deficiency reserve.

Property, furniture, fixtures, equipment and leasehold improvements: Property and equipment are carried at cost less accumulated depreciation. The Company provides for depreciation of property and equipment using the straight-line method over the estimated useful lives of the assets. Furniture and fixtures are generally depreciated over 3 to 10 years. Depreciation expense was $65,885 and $52,116, respectively, for the years ended December 31, 2013 and 2012. Certain property and equipment is nonadmitted through a charge against capital and surplus. Maintenance and repairs are charged to expense as incurred.

Federal income taxes: Current income taxes incurred are recognized in the statutory statements of operations based on tax returns for the current year and tax contingencies for the current and all prior years, to the extent not previously provided.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the statutory financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Gross deferred tax assets and liabilities are measured using enacted tax rates and are considered for admitted asset status according to the admissibility tests as set forth by the NAIC. Changes in deferred tax assets and deferred tax liabilities, including changes attributable to changes in tax rates, are recognized as a component of unassigned surplus.

Gross deferred income tax assets are reduced by a valuation allowance if the Company determines it is more likely than not that some portion or all of the gross deferred tax assets will not be realized. Adjusted deferred income tax assets are limited to (1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse during a timeframe corresponding with IRS tax loss carryback provisions, not to exceed three years, plus (2) the lesser of the remaining gross deferred income tax assets expected to be realized within three years of the balance sheet date or 15% of capital and surplus (subject to certain limitations), excluding any net deferred income tax assets, electronic data processing equipment and operating software and any net positive goodwill, plus (3) the amount of remaining gross deferred income tax assets that can be offset against existing deferred income tax liabilities. The remaining deferred income tax assets in excess of the above are non-admitted. Deferred income taxes do not include amounts for state taxes.

Asset Valuation Reserve and Interest Maintenance Reserve: An Asset Valuation Reserve (AVR) is maintained as prescribed by the NAIC for the purpose of stabilizing the surplus of the Company against fluctuations in the market value of assets.

An Interest Maintenance Reserve (IMR) is maintained as prescribed by the NAIC for the purpose of stabilizing the surplus of the Company against gains and losses on sales of fixed income investments that are primarily attributable to changing interest rates. The interest-related gains and losses are deferred and amortized into income over the remaining term of the securities that were sold.

Note 2. Summary of Significant Accounting Policies (Continued)

Fair values of financial instruments: The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

- *Cash and Short-Term Investments* – The carrying amounts for these instruments approximate their fair values due to their short duration to maturity.

- *Bonds* – The fair values for bonds are based on NAIC-prescribed market values or quoted market prices, where available.

- *Preferred Stocks and Common Stocks of Nonaffiliates* – The fair values are based on quoted market prices.

- *Common Stocks of Affiliates* – The fair values of common stocks of affiliates approximate carrying value and are invested in privately-held life insurance companies. These securities have no active trading. The carrying value of common stocks of affiliates is recorded as the underlying equity of affiliates.

- *Policy Loans* – Policy loans are stated at unpaid principal balances.

- *Mortgage Loans on Real Estate* – The fair values of mortgage loans on real estate, held for investment are estimated by discounting scheduled cash flows through the scheduled maturities of the loans, using interest rates currently being offered for similar loans to borrowers with similar credit ratings. As part of the Old Reliance purchase agreement, the seller guaranteed the performance of the mortgage loans and accordingly the Company believes book value is equal to fair value. The Company periodically evaluates the financial condition of the seller and his guarantee. The Company knows of no circumstances that indicated that the guarantor would be unable to perform nor are any loans non-performing such that his guarantee would be triggered.

- *Liability for Deposit-Type Contracts* – The carrying values of the liability for deposit-type contracts is assumed to be fair value. The Company does not believe an estimate of the fair value of the liability for deposit-type contracts can be made without incurring excessive costs. Because of the numerous assumptions that would have to be made to estimate fair value, the Company believes that such information would not be meaningful.

Note 3. Investments

The amortized cost and estimated fair value of investments in investment securities are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2013:				
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$ 1,120,381	$ 108,137	$ -	$ 1,228,518
States and political subdivisions – general obligations	932,675	-	86,235	846,440
States and political subdivisions – special revenue	888,401	-	65,645	822,756
Corporate and miscellaneous securities	7,309,717	27,657	494,385	6,842,989
	$ 10,251,174	$ 135,794	$ 646,265	$ 9,740,703
Common stock of affiliates	$ 2,062,142	$ -	$ 421,503	$ 1,640,639
Preferred stock	$ 75,000	$ -	$ -	$ 75,000

Note 3. Investments (Continued)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2012:				
U.S. Treasury securities and obligations of U.S. government corporations and agencies	$ 1,338,720	$ 159,570	$ -	$ 1,498,290
States and political subdivisions – general obligations	945,083	1,419	16,379	930,123
States and political subdivisions – special revenue	1,176,182	201	34,697	1,141,686
Corporate and miscellaneous securities	4,940,556	21,458	108,389	4,853,625
	$ 8,400,541	$ 182,648	$ 159,465	$ 8,423,724
Common stock of affiliates	$ 1,873,877	$ -	$ 285,102	$ 1,588,775
Common stock of nonaffiliates	135,800	-	32,148	103,652
	$ 2,009,677	$ -	$ 317,250	$ 1,692,427
Preferred stock	$ 75,000	$ -	$ -	$ 75,000

Note 3. Investments (Continued)

The following tables present the estimated fair value and the gross unrealized losses, aggregated by investment category and length of time that individual investment securities have been in an unrealized loss position, at December 31, 2013 and 2012:

	Investments with Unrealized Losses					
	Less than 12 Months		**Greater than 12 Months**		**Total**	
December 31, 2013:	**Estimated Fair Value**	**Unrealized Losses**	**Estimated Fair Value**	**Unrealized Losses**	**Estimated Fair Value**	**Unrealized Losses**
Bonds:						
States and political subdivisions – general obligation	**$ 174,947**	**$ 19,392**	**$ 671,493**	**$ 66,843**	**$ 846,440**	**$ 86,235**
States and political subdivisions – special revenue	**22,261**	**3,418**	**800,495**	**62,227**	**822,756**	**65,645**
Corporate and miscellaneous securities	**6,560,629**	**494,385**	**-**	**-**	**6,560,629**	**494,385**
	$ 6,757,837	**$ 517,195**	**$ 1,471,988**	**$ 129,070**	**$ 8,229,825**	**$ 646,265**

	Investments with Unrealized Losses					
	Less than 12 Months		Greater than 12 Months		Total	
December 31, 2012:	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Bonds:						
States and political subdivisions – general obligation	$ 621,353	$ 8,963	$ 227,236	$ 7,416	$ 848,589	$ 16,379
States and political subdivisions – special revenue	858,902	26,043	202,562	8,654	1,061,464	34,697
Corporate and miscellaneous securities	2,844,197	108,389	-	-	2,844,197	108,389
	$ 4,324,452	$ 143,395	$ 429,798	$ 16,070	$ 4,754,250	$ 159,465
Common stock of nonaffiliates	$ -	$ -	$ 103,652	$ 32,148	$ 103,652	$ 32,148
	$ -	$ -	$ 103,652	$ 32,148	$ 103,652	$ 32,148

Note 3. Investments (Continued)

The majority of the unrealized losses on securities is due to interest rate changes and market segments that are experiencing temporary value declines. The Company regularly monitors its investment portfolio for securities where the unrealized losses may indicate an other-than-temporary impairment (OTTI) in the value of its securities. This review for impairment considers a number of qualitative and quantitative factors, as well as significant management judgment. There were no realized losses due to OTTI at December 31, 2013 and 2012.

The amortized cost and estimated fair value of debt securities at December 31, 2013, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Statement Value	Estimated Fair Value
Due in one year or less	$ 201,546	$ 211,376
Due after one year through five years	1,337,191	1,341,496
Due after five years through ten years	6,334,614	6,034,216
Due after ten years through twenty years	2,377,823	2,153,615
Due after twenty years	-	-
	$ 10,251,174	$ 9,740,703

Net investment income reflected in the results of operations for the years ended December 31, 2013 and 2012 are as follows:

	2013	2012
Bonds	**$ 319,360**	$ 317,336
Cash and short-term investments	**27**	550
Preferred stock	**94**	2,071
Common stock	**69**	1,109
Mortgage loans	**58,781**	49,747
Real estate	**37,500**	52,500
Contract loans and policy interest	**36,353**	27,719
	452,184	451,032
Less investment expenses	**(32,066)**	(24,163)
	$ 420,118	$ 426,869

Note 3. Investments (Continued)

Gross realized gains and losses from investment securities consist of the following:

Year Ended December 31, 2013	**Gross Realized Gains**	**Gross Realized Losses**	**Net Realized Gains (Losses)**
Bonds	**$ 68,388**	**$ (30,266)**	**$ 38,122**
Common stock of affiliates	**-**	**(15,049)**	**(15,049)**
Other invested assets	**5,109**	**-**	**5,109**
	$ 73,497	**$ (45,315)**	**$ 28,182**
Transfer to IMR			**(19,060)**
Net realized capital gains			**$ 9,122**

Year Ended December 31, 2012	Gross Realized Gains	Gross Realized Losses	Net Realized Gains (Losses)
Bonds	$ 201,942	$ (30,659)	$ 171,283
Common stock of affiliates	-	(3,880)	(3,880)
Preferred stock	2,573	(307)	2,266
	$ 204,515	$ (34,846)	$ 169,669
Transfer to IMR			(171,283)
Net realized capital losses			$ (1,614)

Proceeds from sales of investments during 2013 and 2012 were $5,127,768 and $11,662,813, respectively.

Bonds and other invested assets with a statement value of $1,604,624 and $1,800,488 were on deposit at December 31, 2013 and 2012, respectively, with various banks, as required by the respective states or by reinsurance contracts.

Note 4. Investments in Affiliates

The carrying value of the common stock of affiliates owned by the Company as of December 31, 2013 and 2012 is as follows:

	2013	2012
Capital Reserve Life Insurance Company	**$ 1,424,856**	$ 1,588,775
Midwest Holding Inc.	**215,783**	-
	$ 1,640,639	$ 1,588,775

The Company owns 100% of Capital Reserve. Summarized financial statement information of Capital Reserve as of and for the years ended December 31, 2013 and 2012 is as follows.

Statutory Statement of Admitted Assets, Liabilities and Capital and Surplus	2013	2012
Total Admitted Assets	**$ 1,283,300**	$ 1,412,291
Total Liabilities	**$ 23,554**	$ 16,144
Total Capital and Surplus	**1,259,746**	1,396,147
	$ 1,283,300	$ 1,412,291

Statutory Statements of Operations	2013	2012
Total Revenues	**$ 36,773**	$ 53,463
Total Underwriting Deductions	**147,898**	120,194
Net Realized Loss on Investments	**(4,759)**	(84)
Total Federal Income Taxes	**-**	-
Net Loss	**$ (115,884)**	$ (66,815)

The change in the carrying value of the Company's wholly owned subsidiaries, which includes goodwill, for years ended December 31, 2013 and 2012 follows:

	December 31, 2013		
	Capital and Surplus	**Goodwill**	**Total**
Beginning of year	**$ 1,396,147**	**$ 192,628**	**$ 1,588,775**
Net loss	**(115,884)**	**-**	**(115,884)**
Change in nonadmitted assets	**5,364**	**-**	**5,364**
Change in AVR	**71**	**-**	**71**
Unrealized loss on common stock of affiliate	**(21,224)**		**(21,224)**
Amortization of goodwill	**-**	**(27,518)**	**(27,518)**
Other	**(4,728)**		**(4,728)**
	(136,401)	**(27,518)**	**(163,919)**
End of year	**$ 1,259,746**	**$ 165,110**	**$ 1,424,856**

Note 4. Investments in Affiliates (Continued)

	December 31, 2012		
	Capital and Surplus	Goodwill	Total
Beginning of year	$ 1,406,168	$ 673,797	$ 2,079,965
Net loss	(66,815)	-	(66,815)
Correction of an error	(125,305)	-	(125,305)
Change in deferred tax asset	(451,915)	-	(451,915)
Change in nonadmitted assets	633,637	-	633,637
Write off of Old Reliance goodwill	-	(453,650)	(453,650)
Amortization of goodwill	-	(27,519)	(27,519)
Change in AVR	377	-	377
	(10,021)	(481,169)	(491,190)
End of year	$ 1,396,147	$ 192,628	$ 1,588,775

Note 5. Fair Value of Financial Instruments

The fair values of investment securities, including short-term investments and cash, are estimated based on prices received from SVO and Reference Data. Cash and short-term investment fair values approximate their carrying values. The amortized cost and the estimated fair value of investment securities as of December 31, 2013 and 2012 were as follows:

	2013		2012	
	Statement Value	**Estimated Fair Value**	Statement Value	Estimated Fair Value
Financial assets:				
Bonds	**$ 10,251,174**	**$ 9,740,703**	$ 8,400,541	$ 8,423,724
Common stocks – affiliates	**1,640,639**	**1,640,639**	1,588,775	1,588,775
Common stocks – nonaffiliates	**-**	**-**	103,652	103,652
Preferred stocks	**75,000**	**75,000**	75,000	75,000
Mortgage loans	**642,327**	**690,591**	647,139	706,434
Policy loans	**368,404**	**368,404**	274,664	274,664
Cash	**596,504**	**596,504**	914,345	914,345
Financial liabilities:				
Liability for deposit-type contracts	**369,915**	**369,915**	455,236	455,236

The Company has no other assets or liabilities meeting the definition of a financial instrument. In addition, the Company has no off-balance-sheet financial instruments.

Note 5. Fair Value of Financial Instruments (Continued)

The Company's financial assets and liabilities carried at fair value have been classified, for disclosure purposes, based on a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The hierarchy gives the highest priority to fair values determined using unadjusted quote prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to fair values determined using unobservable inputs (Level 3). An asset's or liability's classification is determined based on the lowest level input that is significant to its measurement. For example, a Level 3 fair value measurement may include inputs that are both observable (Levels 1 and 2) and unobservable (Level 3). The levels of the fair value hierarchy are as follows:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2 – Valuations derived from inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, such as:

a) Quoted prices for similar assets or liabilities in active markets.
b) Quoted prices for identical or similar assets or liabilities in markets that are not active.
c) Inputs other than quoted prices that are observable for the asset or liability.
d) Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 – Valuations are derived from techniques that require significant unobservable inputs. The unobservable inputs reflect the Company's own assumptions about the assumptions that market participants would use in pricing the asset or liability.

The following summarizes financial instruments measured at fair value as of December 31, 2012, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value. There were no financial instruments measured at fair value as of December 31, 2013.

December 31, 2012	Level 1	Level 2	Level 3	Total Estimated Fair Value
Assets at fair value				
Common stock	$ 103,652	$ -	$ -	$ 103,652
Total assets at fair value	$ 103,652	$ -	$ -	$ 103,652

Note 6. Reinsurance

The Company utilizes reinsurance contracts to reduce its exposure to losses in all aspects of its insurance business. Such reinsurance permits recovery of a portion of losses from reinsurers, although it does not relieve the Company from its primary liability to policyholders. Failure of reinsurers to honor their obligations could result in losses to the Company. The Company evaluates the financial strength of potential reinsurers and continually monitors the financial condition of reinsurers.

Amounts recoverable from reinsurers are estimated based upon assumptions consistent with those used in establishing the liabilities related to the underlying reinsured contracts. Management believes the recoverables are appropriately established. The Company generally strives to diversify its credit risks related to reinsurance ceded.

A summary of reinsurance amounts affecting the accompanying statutory financial statements follows:

	2013		2012	
	Written	**Earned**	Written	Earned
Direct	**$ 4,710,181**	**$ 4,710,181**	$ 4,829,659	$ 4,829,659
Assumed	**31,220**	**31,220**	33,644	33,644
Ceded	**(99,397)**	**(99,397)**	(98,798)	(98,798)
Net	**$ 4,642,004**	**$ 4,642,004**	$ 4,764,505	$ 4,764,505

The following table provides a summary of the significant reinsurance balances recoverable on paid and unpaid losses by reinsurers, along with the A.M. Best credit rating:

Reinsurer	Credit Rating	Recoverable on Paid Losses	Recoverable on Unpaid Losses
Optimum Re Insurance Company	A-	$ -	$ 11,000
Sagicor Life Insurance Company	A-	-	230,487
		$ -	$ 241,487

Note 7. Deposit Liabilities

Withdrawal characteristics of deposit-type contracts and other contracts with life contingencies are as follows at December 31, 2013 and 2012:

	2013	2012
Subject to discretionary withdrawal without surrender charge or market value adjustment	**$ 369,915**	$ 455,236
Not subject to withdrawal	**-**	-
Total	**$ 369,915**	$ 455,236

Note 7. Deposit Liabilities (Continued)

The Company holds a reserve for the nondeduction of deferred fractional premiums or return of premium at the death of the insured. Reserves are computed to be never less than the surrender value defined in the policy.

Extra premiums are charged for substandard lives for certain types of policies, plus the gross premium for the true age. Mean reserves are determined by computing the regular mean reserve for the plan and holding, in addition, one-half of the extra premium charged. For the other groups of policies, substandard lives are issued policies with initially reduced death benefit schedules that increase with duration to the ultimate amount. Mean reserves are determined by computing the regular mean reserve for the ultimate face amount.

At December 31, 2013 and 2012, the amount of $369,915 and $455,236, respectively, reported as deposit-type funds, relates to supplemental contracts, dividends, and premiums on deposit and are reported as policyholder funds left on deposit in the statutory statements of admitted assets, liabilities, and surplus.

Note 8. Premiums and Annuity Considerations Deferred and Uncollected

Deferred and uncollected life insurance premiums and annuity considerations as of December 31, 2013 and 2012 were as follows:

	2013		2012	
	Gross	**Net of Loading**	Gross	Net of Loading
Ordinary - first year due and deferred	**$ 35,870**	**$ 13,491**	$ 80,073	$ 30,115
Ordinary - renewal due and deferred	**270,644**	**157,340**	353,372	196,549
Total	**$ 306,514**	**$ 170,831**	$ 433,445	$ 226,664

Note 9. Transactions with Parent Company

The Company has a cost sharing agreement with its parent company Midwest Holding Inc. Under the terms of this cost sharing agreement, the Company paid Midwest Holding Inc. the amount of $734,641 and $1,240,539 and had a receivable of $147,197 and $33,761 for the years ended December 31, 2013 and 2012, respectively. These transactions are settled monthly.

Note 10. Income Taxes

At December 31, the components of the net adjusted admitted deferred income tax asset were as follows:

	12/31/2013			12/31/2012			Change		
	Ordinary	Capital	Total	Ordinary	Capital	Total	Ordinary	Capital	Total
Gross deferred tax assets	$ 2,100,511	$ -	$ 2,100,511	$ 2,372,305	$ 10,930	$ 2,383,235	$ (271,794)	$ (10,930)	$ (282,724)
Statutory valuation allowance	2,042,428	-	2,042,428	2,295,239	10,930	2,306,169	(252,811)	(10,930)	(263,741)
Adjusted gross deferred tax assets	58,083	-	58,083	77,066	-	77,066	(18,983)	-	(18,983)
Deferred tax assets nonadmitted	-	-	-	-	-	-	-	-	-
Net admitted deferred tax asset	58,083	-	58,083	77,066	-	77,066	(18,983)	-	(18,983)
Deferred tax liabilities	58,083	-	58,083	77,066	-	77,066	(18,983)	-	(18,983)
Net adjusted deferred tax asset	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -

At December 31, 2013 and 2012, the Company recorded a valuation allowance on the deferred tax assets to reduce the total to an amount that management believes will ultimately be realized. Realization of deferred tax assets is dependent upon sufficient future taxable income during the period that deductible temporary differences and carryforwards are expected to be available to reduce taxable income.

The significant components, by character, of deferred tax assets and liabilities as of December 31, 2013 and 2012, were as follows:

	December 31, 2013			
	Statutory	**Tax**	**Difference**	**Tax Effect**
Deferred tax assets - ordinary				
Net operating loss carry forward	**$ -**	**$ 5,486,483**	**$ 5,486,483**	**$ 1,865,404**
Deferred acquisition costs	**-**	**597,248**	**597,248**	**203,064**
Other	**-**	**94,243**	**94,243**	**32,043**
Total deferred tax assets - ordinary				**2,100,511**
Deferred tax assets - capital				
Unrealized loss on common stock of nonaffilates	**-**	**-**	**-**	**-**
Total deferred tax assets - capital				**-**
Total gross deferred tax assets				**2,100,511**
Statutory valuation allowance				**(2,042,428)**
Total adjusted deferred tax assets				**58,083**
Deferred tax liabilities - ordinary				
Due and deferred premiums	**170,831**	**-**	**170,831**	**58,083**
Total gross deferred tax liabilities				**58,083**
Total net deferred tax asset				**-**
Nonadmitted deferred tax asset				**-**
Total net admitted deferred tax asset				**$ -**

Note 10. Income Taxes (Continued)

	December 31, 2012			
	Statutory	Tax	Difference	Tax Effect
Deferred tax assets - ordinary				
Net operating loss carry forward	$ -	$ 6,182,462	$ 6,182,462	$ 2,102,037
Deferred acquisition costs	-	672,325	672,325	228,591
Other	-	122,578	122,578	41,677
Total deferred tax assets - ordinary				2,372,305
Deferred tax assets - capital				
Unrealized loss on common stock of nonaffilates	103,652	135,800	32,148	10,930
Total deferred tax assets - capital				10,930
Total gross deferred tax assets				2,383,235
Statutory valuation allowance				(2,306,169)
Total adjusted deferred tax assets				77,066
Deferred tax liabilities - ordinary				
Due and deferred premiums	226,664	-	226,664	77,066
Total gross deferred tax liabilities				77,066
Total net deferred tax asset				-
Nonadmitted deferred tax asset				-
Total net admitted deferred tax asset				$ -

The change in deferred income taxes reported in surplus comprises the following components:

	2013	2012	Change
Deferred tax assets - ordinary:			
Net operating loss carry forward	**$ 1,865,404**	$ 2,102,037	$ (236,633)
Deferred acquisition costs	**203,064**	228,591	(25,527)
Other	**32,043**	41,677	(9,634)
Total deferred tax assets - ordinary	**2,100,511**	2,372,305	(271,794)
Deferred tax assets - capital:			
Unrealized loss on common stock of nonaffiliates	**-**	10,930	(10,930)
Total deferred tax assets	**2,100,511**	2,383,235	(282,724)
Statutory valuation allowance	**(2,042,428)**	(2,306,169)	263,741
Total adjusted deferred tax assets	**58,083**	77,066	(18,983)
Deferred tax liabilities - ordinary:			
Due and deferred premiums	**58,083**	77,066	(18,983)
Other	**-**	-	-
Total deferred tax liabilities	**58,083**	77,066	(18,983)
Total net deferred tax asset	**$ -**	$ -	$ -
Nonadmitted deferred tax asset	**-**	-	-
Total net admitted deferred tax asset	**$ -**	$ -	$ -

Note 10. Income Taxes (Continued)

Current income taxes incurred consist of the following major components:

Current year tax expense (benefit)		**2013**		2012
Federal income tax (benefit)	**$**	**263,741**	$	(334,886)
Change in statutory valuation allowance		**(263,741)**		334,886
Current income tax (benefit)	**$**	**-**	$	-

The Company's income tax incurred and change in deferred income tax differ from the amount obtained by applying the federal statutory rate of 34% to income before income taxes, as follows:

		2013		2012
Current income tax (benefit) incurred	**$**	**-**	$	-
Deferred tax expense		**-**		-
Total income tax reported	**$**	**-**	$	-
Net loss before income taxes and before capital gains tax	**$**	**(20,497)**	$	(911,049)
		34%		34%
Expected income tax expense at 34% statutory rate		**(6,969)**		(309,757)
Increase (decrease) in actual tax reported resulting from:				
Change in valuation allowance		**(263,741)**		334,886
Deferred tax adjustment		**47,654**		-
Meals and entertainment		**9,830**		-
Change in net operating loss		**241,776**		-
Amortization of IMR		**(11,076)**		-
Other		**(17,474)**		(25,129)
Current income tax reported	**$**	**-**	$	-

As of December 31, 2013, the Company has operating loss carryforwards of $5,486,483 that will expire from 2024 through 2028.

As of December 31, 2013 and 2012, there were no federal income taxes incurred that are available for recoupment of future net losses, there were no deferred tax liabilities that were not recognized in determining the net admitted deferred tax asset, the Company did not employ any tax planning strategies, and the Company does not have any tax loss contingencies for which it is reasonably possible that the total liability will significantly increase within 12 months of the reporting date.

Note 11. Commitments and Contingencies

The Company is a party to certain claims and legal actions arising during the ordinary course of business. It is management's opinion, after consulting with legal counsel, that these matters will not have a material adverse effect on the financial position and results of operations of the Company.

Note 12. Surplus Notes

The following table provides a summary of the Company's surplus notes along with issue dates, maturity dates, face amounts, and interest rates as of December 31, 2013:

Creditor	Issue Date	Maturity Date	Face Amount	Interest Rate
First American Capital Corporation	September 1, 2006	September 1, 2016	$ 250,000	7%
David G. Elmore	August 4, 2011	August 1, 2016	$ 300,000	5%

Any payments and/or repayments must be approved by the Arizona Department of Insurance. On April 2, 2012, the Company paid down $300,000 of principal and approximately $50,000 of accrued interest. During the first quarter of 2013, the repayment of the interest and principal on a portion of the surplus notes was approved by the Arizona Department of Insurance. On January 4, 2013, the Company paid down $100,000 of principal and approximately $7,000 of accrued interest.

Note 13. Subsequent Events

All of the effects of subsequent events that provide additional evidence about conditions that existed at the statements of admitted assets, liabilities, capital and surplus date, including the estimates inherent in the process of preparing the statutory financial statements, are recognized in the statutory financial statements. The Company does not recognize subsequent events that provide evidence about conditions that did not exist at the Statements of Admitted Assets, Liabilities, Capital and Surplus date but arose after, but before the statutory financial statements are available to be issued. In some cases, nonrecognized subsequent events are disclosed to keep the statutory financial statements from being misleading.

Subsequent events have been evaluated through June 26, 2014, the date that the statutory financial statements were issued.

Note 14. Reconciliation to Annual Statement

For 2013, The Company recorded adjustments to common stocks, interest and dividends due and accrued, premiums and considerations, accrued expenses and taxes, premiums earned, investment income earned, commissions, and general expenses in the 2013 audited financial statements which were not recorded in the 2013 annual statement.

Note 14. Reconciliation to Annual Statement (Continued)

The following table shows the difference in the annual statement filed with the Insurance Department of the State of Arizona and the audited statutory statements of admitted assets, liabilities and capital and surplus and the statutory statements of operations for the year ended December 31, 2013.

	Annual Statement	Difference	Audited Financial Statements
Statutory Statements of Admitted Assets,			
Liabilities, and Capital Stock and Surplus			
Common stocks	$ 1,777,040	$ (136,401)	$ 1,640,639
Interest and dividends due and accrued	86,856	31,418	118,274
Premiums and considerations	157,363	13,468	170,831
Accrued expenses and taxes	160,598	(116,286)	44,312
Unassigned deficit	(9,734,792)	24,771	(9,710,021)
Statutory Statements of Operations			
Premiums earned	$ 4,628,536	$ 13,468	$ 4,642,004
Investment income earned, net of investment expenses			
of $32,066 and $24,163, respectively	388,700	31,418	420,118
Commissions	595,238	(55,739)	539,499
General expenses	1,300,129	(33,249)	1,266,880
Net loss	(154,371)	133,874	(20,497)

AMERICAN LIFE & SECURITY CORP. **Schedule 1**

Selected Financial Data

Year Ended December 31, 2013

Investment income earned:		
Government bonds	$	50,866
Other bonds (unaffiliated)		268,494
Bonds of affiliates		-
Preferred stocks (unaffiliated)		94
Common stocks (unaffiliated)		69
Common stocks of affiliates		-
Mortgage loans		58,781
Real estate		37,500
Premium notes, policy loans, and liens		36,353
Cash on hand and on deposit		27
Short-term investments		-
Other invested assets		-
Derivative instruments		-
Aggregate write-ins for investment		-
Gross investment income	$	452,184
Real estate owned - book value less encumbrances	$	-
Mortgage loans - book value:		
Farm mortgages	$	-
Residential mortgages		642,327
Commercial mortgages		-
Total mortgage loans	$	642,327
Mortgage loans, by standing - book value		
Good standing	$	-
Good standing with restructured terms		-
Interest overdue more than three months, not in foreclosure		-
Foreclosure in process		-
Other long-term assets - statement value		-
Collateral loans		-
Bonds and stocks of parents, subsidiaries, and affiliates - book value:		
Bonds		-
Preferred stocks		-
Common stocks		1,640,639
Bonds and short-term investments, by maturity and class:		
By maturity - statement value:		
Due within 1 year or less		201,546
Over 1 year through 5 years		1,337,191
Over 5 years through 10 years		6,334,614
Over 10 years through 20 years		2,377,823
Over 20 years		-
Total bonds and short-term investments by maturity	$	10,251,174

(Continued)

By class - statement value:	
Class 1	$ 8,467,566
Class 2	1,783,608
Class 3	-
Class 4	-
Class 5	-
Class 6	-
Total bonds and short-term investments by class	$ 10,251,174
Total bonds publicly traded	$ 10,251,174
Total bonds privately placed	$ -
Preferred stocks - statement value	$ 75,000
Common stocks - market value	-
Short-term investments - book value	-
Options, caps, and floors owned - statement value	-
Options, caps, and floors written and in force - statement value	-
Collars, swap, and forward agreements open - statement value	-
Futures contracts open - current value	-
Cash on deposit	596,504
Life insurance in force (in thousands):	
Industrial	$ 5,173
Ordinary	188,704
Credit life	-
Group life	-
Amount of accidental death insurance in force under ordinary policies (in thousands)	$ -
Life insurance policies with disability provisions in force (in thousands):	
Industrial	$ -
Ordinary	-
Credit life	-
Group life	-
Supplementary contracts in force:	
Ordinary - not involving life contingencies:	
Amount of deposit	$ -
Income payable	-
Ordinary - involving life contingencies:	
Amount of deposit	-
Income payable	-
Group - not involving life contingencies:	
Amount of deposit	-
Income payable	-
Group - involving life contingencies:	
Income payable	-

(Continued)

Annuities:		
Ordinary:		
Immediate - amount of income payable	$	-
Deferred - fully paid account balance		382,754
Deferred - not fully paid account balance		3,810,673
Group:		
Amount of income payable		-
Fully paid account balance		-
Not fully paid account balance		-
Accident and health insurance - premiums in force:		
Ordinary	$	-
Group		-
Credit		-
Deposit funds and dividend accumulations:		
Deposit funds - account balance	$	369,915
Dividend accumulations - account balance		-
Claim payments - years ended December 31 (in thousands):		
Group accident and health:		
2013	$	-
2012		-
2011		-
2010		-
2009		-
Prior		-
Other accident and health:		
2012	$	10,027
2011		7,146
2010		10,083
2009		21,140
2008		24,296
Prior		38,581
Other coverages that use developmental methods to calculate claim reserves:		
2013	$	-
2012		-
2011		-
2010		-
2009		-
Prior		-

See accompanying Independent Auditor's Report.

AMERICAN LIFE & SECURITY CORP. **Schedule 2**

Supplemental Investment Risks Interrogatories

Year Ended December 31, 2013

1. Admitted assets per Annual Statement	$ 14,781,743

2. The 10 largest exposures to single issuer/borrower/investment, by investment category, excluding (i) U.S. government, U.S. government agency securities, and those U.S. government money market funds listed in the Appendix to the SVO Purposes and Procedures Manual as exempt, (ii) property occupied by the Company, and (iii) policy loans, at December 31, 2013 are as follows:

Issuer	Category	Amount	Percentage of total admitted assets
Capital Reserve Life Insurance Company	Wholly owned insurance subsidiary	$ 1,424,856	9.64%
Wells Fargo & Company	Corporate	366,780	2.48%
Maricopa County, Arizona	States and Political Subdivisions – General Obligation	341,390	2.31%
Proassurance Group	Corporate	319,700	2.16%
JP Morgan Chase & Co.	Corporate	318,542	2.15%
Bank of America Corp.	Corporate	296,990	2.01%
Nationsbank Corp.	Corporate	245,566	1.66%
Wayne County, Michigan	States and Political Subdivisions – General Obligation	232,951	1.58%
Axis Specialty Finance	Corporate	229,242	1.55%
Convention Center Authority RI	Corporate	228,808	1.55%

3. As of December 31, 2013, the amounts and percentages of total admitted assets held in bonds, including those classified as short-term investments, and preferred stocks by NAIC rating are as follows:

Investment category	**Amount**	**Percentage of total admitted assets**
NAIC—1	$ 8,467,566	57.28%
NAIC—2	1,783,608	12.07
NAIC—3	—	—
NAIC—4	—	—
NAIC—5	—	—
NAIC—6	—	—

4. As of December 31, 2013, the Company does not hold foreign investments that exceed 2.5% of admitted assets. Therefore, interrogatories 5-10 are not applicable.

11. As of December 31, 2013, the Company does not hold Canadian investments and unhedged Canadian currency exposures, including Canadian-currency-denominated investments that exceed 2.5% of total admitted assets.

12. As of December 31, 2013, the Company does not hold investments with contractual sales restrictions (defined as investments having restrictions that prevent investments from being sold within 90 days at December 31, 2013).

(Continued)

13. The largest exposures to equity interest as of December 31, 2013 are as follows:

Issuer	Amount	Percentage of total admitted assets
Capital Reserve Life Insurance Company	$ 1,424,856	9.64%
Midwest Holding Inc.	215,783	1.46%
Allinazgi CVT & INC FR II	25,000	0.17%
Allinazgi CVT & INC Fund	25,000	0.17%
Pimco Corp Income Fund	25,000	0.17%

14. As of December 31, 2013, the Company held no investments in nonaffiliated, privately placed equities (included in other equity securities), excluding securities eligible for sale under (i) Securities and Exchange Commission ("SEC") Rule 144a or (ii) SEC Rule 144 without volume restrictions.

15. As of December 31, 2013, the Company held no investments in general partnership interests (included in other equity securities).

16. The type of mortgage loans held as of December 31, 2013 are as follows:

Type	Amount	Percentage of total admitted assets
Residential mortgages	$ 642,327	4.35%
Construction loans	$ -	0.00%
Mortgage loans over 90 days past due	-	0.00%
Mortgage loans in the process of foreclosure	-	0.00%
Mortgage loans foreclosed	-	0.00%
Restructured mortgage loans	-	0.00%

17. The aggregate loan-to-value ratios as determined from the most current appraisal as of December 31, 2013 are as follows:

Loan-to-Value	Amount	Percentage of total admitted assets
Above 95%	$ -	0.00%
91% to 95%	-	0.00%
81 to 90%	-	0.00%
71 to 80%	510,375	3.45%
below 70%	131,952	0.89%

18. The largest five investments in any one parcel or group of contiguous parcels of real estate as of December 31, 2013 are as follows:

Description	Amount	Percentage of total admitted assets
1946 Ala Moana Blvd, Honolulu, Hawaii (10 Units)	$ 553,849	3.75%

19. As of December 31, 2013, the Company does not hold investment in mezzanine real estate loans that exceed 2.5% total admitted assets.

See accompanying Independent Auditor's Report.

AMERICAN LIFE & SECURITY CORP. **Schedule 3**

Summary Investment Schedule

December 31, 2013

Investment categories	Gross investment holdings Amount	Gross investment holdings Percentage	Admitted assets as reported in the Annual Statement Amount	Admitted assets as reported in the Annual Statement Percentage
Bonds:				
U.S. Treasury securities	$ 1,120,381	7.9%	$ 1,120,381	7.9%
U.S. government and corporate obligations (excluding mortgage-backed securities):				
Issued by U.S. government agencies	—	—	—	—
Issued by U.S. government-sponsored agencies	—	—	—	—
Foreign government (including Canada; excluding mortgage-backed securities)	—	—	—	—
Securities issued by states, territories and possessions, and political subdivisions in the U.S.:				
States, territories, and possessions general obligations	932,675	6.6	932,675	6.6
Political subdivision of states, territories and possessions, and political subdivisions general obligations	—	—	—	—
Revenue and assessment obligations	888,401	6.3	888,401	6.3
Industrial development and similar obligations	7,309,717	51.7	7,309,717	51.7
Mortgage-backed securities (including residential and commercial MBS):				
Pass-through securities:				
Guaranteed by GNMA	—	—	—	—
Issued by FNMA and FHLMC	—	—	—	—
Privately issued	—	—	—	—
CMOs and REMICs:				
Issued by FNMA and FHLMC	—	—	—	—
Privately issued and collateralized by MBS; issued or guaranteed by GNMA, FNMA, or FHLMC	—	—	—	—
All other privately issued	—	—	—	—
Other debt and other fixed income securities (excluding short-term):				
Unaffiliated domestic securities (includes credit tenant loans rated by the SVO)	—	—	—	—
Unaffiliated foreign securities	—	—	—	—
Affiliated securities	—	—	—	—
Equity interests:				
Investments in mutual funds	—	—	—	—
Preferred stocks:				
Affiliated	—	—	—	—
Unaffiliated	75,000	0.5	75,000	0.5
Publicly traded equity securities (excluding preferred stocks):				
Affiliated	—	—	—	—
Unaffiliated	—	—	—	—
Other equity securities:				
Affiliated	1,640,639	11.6	1,640,639	11.6
Unaffiliated	—	—	—	—
Other equity interests, including tangible personal property under lease:				
Affiliated	—	—	—	—
Unaffiliated	—	—	—	—

(Continued)

AMERICAN LIFE & SECURITY CORP. **Schedule 3**

Summary Investment Schedule (Continued)

December 31, 2013

Investment categories	Gross investment holdings Amount	Gross investment holdings Percentage	Admitted assets as reported in the Annual Statement Amount	Admitted assets as reported in the Annual Statement Percentage
Mortgage loans:				
Construction and land development	—	—	—	—
Agricultural	—	—	—	—
Single family residential properties	665,569	4.7	642,327	4.5
Multifamily residential properties	—	—	—	—
Commercial loans	—	—	—	—
Real estate investments:				
Property occupied by Company	—	—	—	—
Property held for production of income (includes $0 of property acquired in satisfaction of debt)	553,849	3.9	553,849	3.9
Property held for sale ($0 including property acquired in satisfaction of debt)	—	—	—	—
Policy loans	368,404	2.6	368,404	2.6
Receivables for securities	—	—	—	—
Cash and short-term investments	596,504	4.2	596,504	4.2
Other invested assets	—	—	—	—
Total invested assets	$ 14,151,139	100.0%	$ 14,127,897	100.0%

See accompanying Independent Auditors' Report.