

**CITIZENS, INC.**

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The laws and regulations of the jurisdictions in which our U.S. insurance subsidiaries are domiciled require that a controlling party obtain the approval of the insurance commissioner of the insurance company's jurisdiction of domicile prior to acquiring control of the insurer and may delay, deter or prevent a transaction our shareholders might consider desirable.

Risk-based capital ("RBC") requirements are imposed on life and property and casualty insurance companies. The NAIC has established minimum capital requirements in the form of RBC. RBC requirements weight the type of business underwritten by an insurance company, the quality of its assets, and various other aspects of an insurance company's business to develop a minimum level of capital called "authorized control level risk-based capital" and compares this level to adjusted statutory capital that includes capital and surplus as reported under statutory accounting principles, plus certain investment reserves. Should the ratio of adjusted statutory capital to control level risk-based capital fall below 200%, a series of actions would be required by the affected company, including submitting a capital plan to the Department of Insurance in the insurance company's state of domicile.

**INTERNATIONAL REGULATION**

CICA Ltd., our Bermuda domiciled subsidiary, is subject to regulation and supervision by the Bermuda Monetary Authority (the "BMA") and compliance with all applicable Bermuda law and Bermuda insurance statutes and regulations, including but not limited to Bermuda's Insurance Act 1978 (the "Insurance Act").

CICA Ltd., which is incorporated to conduct long-term business, is registered as a Class E insurer, which is the license class for long-term insurers and reinsurers with total assets of more than \$500 million that are not registrable as a single-parent or multi-owner long-term captive insurer or reinsurer. CICA Ltd. is not licensed to conduct any business other than an insurance business. The Insurance Act regulates the insurance business of CICA Ltd. and provides that no person may conduct any insurance business in or within Bermuda unless registered as an insurer under the Insurance Act by the BMA.

The Insurance Act imposes solvency and liquidity standards as well as auditing and reporting requirements and confers on the BMA powers to supervise, investigate and intervene in the affairs of insurance companies. Certain requirements of the Insurance Act include: the filing of annual statutory financial returns; the filing of annual U.S. GAAP financial statements; the filing of an annual capital and solvency return; the delivery of a declaration of compliance; compliance with minimum enhanced capital requirements; compliance with the BMA's Insurance Code of Conduct; compliance with minimum solvency margins; limitations on dividends and distributions that CICA Ltd. may make to Citizens, Inc., its parent company; preparation of an annual Financial Condition Report providing details of measures governing the business operations, corporate governance framework, solvency and financial performance; preparation of an assessment of an insurer's own risk and solvency requirements, referred to as a Commercial Insurer's Solvency Self-Assessment; the establishment and maintenance of a head and principal office in Bermuda (with certain officers, a principal representative and a director to reside in Bermuda); appointment of an independent auditor; appointment of an actuary approved by the BMA; and compliance with restrictions on certain changes in control of regulated insurers.

Bermuda's regulatory regime provides a risk-based capital model, termed the Bermuda Solvency Capital Requirement ("BSCR"), as a tool to assist the BMA both in measuring risk and in determining appropriate levels of capitalization. The BSCR employs a standard mathematical model that correlates the risk underwritten by Bermuda insurers to their capital. The BSCR framework applies a standard measurement format to the risk associated with an insurer's assets, liabilities and premiums, including a formula to take into account catastrophe risk exposure. The BMA established risk-based regulatory capital adequacy and solvency margin requirements for Bermuda insurers mandate that a Bermuda domiciled subsidiary's Enhanced Capital Requirement ("ECR") be calculated by either (a) BSCR, or (b) an internal capital model which the BMA has approved for use for this purpose. CICA Ltd. uses the BSCR in calculating its solvency requirements. The Economic Balance Sheet ("EBS") framework is embedded as part of the BSCR and forms the basis of our ECR.

In order to minimize the risk of a shortfall in capital arising from an unexpected adverse deviation, and to facilitate the implementation of a risk-based capital approach, the BMA has established a threshold capital level (termed the Target Capital Level ("TCL")), set at 120% of ECR, that serves as an early warning tool for the BMA. Failure to maintain statutory capital at least equal to the TCL would likely result in increased BMA regulatory oversight.