

United States  
Securities and Exchange Commission  
Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

☒ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange act of 1934**

For the quarterly period ended September 30, 2016

☐ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period From \_\_\_\_\_ to \_\_\_\_\_ .

Commission file number: **000-52613**

**FIRST TRINITY FINANCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

**Oklahoma**

(State or other jurisdiction of incorporation or organization)

**34-1991436**

(I.R.S. Employer Identification Number)

**7633 East 63rd Place, Suite 230**

**Tulsa, Oklahoma 74133-1246**

(Address of principal executive offices)

**(918) 249-2438**

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer: ☐ Accelerated filer: ☐ Non-accelerated filer: ☐ Smaller reporting company: ☒

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

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date:  
Common stock .01 par value as of November 7, 2016: 7,802,593 shares

**FIRST TRINITY FINANCIAL CORPORATION  
QUARTERLY REPORT ON FORM 10-Q  
FOR QUARTERLY PERIOD ENDED SEPTEMBER 30, 2016**

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## PART I – FINANCIAL INFORMATION

### Item 1. Consolidated Financial Statements

First Trinity Financial Corporation and Subsidiaries  
Consolidated Statements of Financial Position

	September 30, 2016 (Unaudited)	December 31, 2015
<b>Assets</b>		
Investments		
Available-for-sale fixed maturity securities at fair value (amortized cost: \$128,986,347 and \$138,028,455 as of September 30, 2016 and December 31, 2015, respectively)	\$ 134,592,061	\$ 134,556,027
Available-for-sale equity securities at fair value (cost: \$683,928 and \$790,215 as of September 30, 2016 and December 31, 2015, respectively)	813,424	892,800
Mortgage loans on real estate	67,897,303	58,774,918
Investment real estate	2,416,063	2,326,558
Policy loans	1,561,972	1,486,317
Short-term investments	50,004	599,855
Other long-term investments	41,658,491	31,566,927
Total investments	248,989,318	230,203,402
Cash and cash equivalents	26,703,311	9,047,586
Accrued investment income	2,148,495	2,205,469
Recoverable from reinsurers	1,281,156	1,243,618
Agents' balances and due premiums	1,414,608	1,070,050
Deferred policy acquisition costs	16,422,517	13,015,679
Value of insurance business acquired	6,007,025	6,288,200
Other assets	10,098,112	6,055,838
<b>Total assets</b>	<b>\$ 313,064,542</b>	<b>\$ 269,129,842</b>
<b>Liabilities and Shareholders' Equity</b>		
Policy liabilities		
Policyholders' account balances	\$ 224,998,722	\$ 197,688,616
Future policy benefits	43,466,880	39,464,124
Policy claims	809,219	714,928
Other policy liabilities	82,185	76,554
Total policy liabilities	269,357,006	237,944,222
Deferred federal income taxes	1,988,584	33,210
Other liabilities	3,205,152	937,367
<b>Total liabilities</b>	<b>274,550,742</b>	<b>238,914,799</b>
<b>Shareholders' equity</b>		
Common stock, par value \$.01 per share (20,000,000 shares authorized, 8,050,173 issued as of September 30, 2016 and December 31, 2015 and 7,802,593 outstanding as of September 30, 2016 and December 31, 2015)	80,502	80,502
Additional paid-in capital	28,684,598	28,684,598
Treasury stock, at cost (247,580 shares as of September 30, 2016 and December 31, 2015)	(893,947)	(893,947)
Accumulated other comprehensive income (loss)	4,510,942	(2,655,817)
Accumulated earnings	6,131,705	4,999,707
<b>Total shareholders' equity</b>	<b>38,513,800</b>	<b>30,215,043</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 313,064,542</b>	<b>\$ 269,129,842</b>

See notes to consolidated financial statements (unaudited).

First Trinity Financial Corporation and Subsidiaries  
Consolidated Statements of Operations  
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
<b>Revenues</b>				
Premiums	\$ 3,197,228	\$ 2,496,403	\$ 9,426,803	\$ 7,141,841
Net investment income	3,303,980	2,916,317	9,922,817	7,828,639
Net realized investment gains	160,308	280,763	307,250	786,852
Loss on other-than-temporary impairment	-	(1,078)	-	(305,334)
Gain on reinsurance assumption	-	38,923	-	588,923
Other income	10,053	40,492	25,259	56,656
<b>Total revenues</b>	<b>6,671,569</b>	<b>5,771,820</b>	<b>19,682,129</b>	<b>16,097,577</b>
<b>Benefits, Claims and Expenses</b>				
Benefits and claims				
Increase in future policy benefits	1,357,212	909,156	3,995,230	2,605,117
Death benefits	881,928	803,941	2,868,216	2,574,150
Surrenders	205,356	122,655	541,725	400,536
Interest credited to policyholders	1,754,941	1,459,480	5,090,162	4,052,780
Dividend, endowment and supplementary life contract benefits	81,040	66,689	214,552	224,793
<b>Total benefits and claims</b>	<b>4,280,477</b>	<b>3,361,921</b>	<b>12,709,885</b>	<b>9,857,376</b>
Policy acquisition costs deferred	(2,023,246)	(1,596,615)	(5,142,381)	(3,819,582)
Amortization of deferred policy acquisition costs	536,901	428,448	1,588,938	1,285,997
Amortization of value of insurance business acquired	91,966	92,561	281,175	291,918
Commissions	1,954,586	1,430,501	4,783,307	3,340,116
Other underwriting, insurance and acquisition expenses	1,244,013	1,189,367	4,123,540	3,599,813
<b>Total expenses</b>	<b>1,804,220</b>	<b>1,544,262</b>	<b>5,634,579</b>	<b>4,698,262</b>
<b>Total benefits, claims and expenses</b>	<b>6,084,697</b>	<b>4,906,183</b>	<b>18,344,464</b>	<b>14,555,638</b>
<b>Income before total federal income tax expense</b>	<b>586,872</b>	<b>865,637</b>	<b>1,337,665</b>	<b>1,541,939</b>
Current federal income tax expense	4,472	218,754	41,982	318,132
Deferred federal income tax expense (benefit)	83,814	(834)	163,685	(157,546)
<b>Total federal income tax expense</b>	<b>88,286</b>	<b>217,920</b>	<b>205,667</b>	<b>160,586</b>
<b>Net income</b>	<b>\$ 498,586</b>	<b>\$ 647,717</b>	<b>\$ 1,131,998</b>	<b>\$ 1,381,353</b>
<b>Net income per common share basic and diluted</b>	<b>\$ 0.06</b>	<b>\$ 0.08</b>	<b>\$ 0.15</b>	<b>\$ 0.18</b>

See notes to consolidated financial statements (unaudited).

First Trinity Financial Corporation and Subsidiaries  
Consolidated Statements of Comprehensive Income (Loss)  
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
<b>Net income</b>	\$ 498,586	\$ 647,717	\$ 1,131,998	\$ 1,381,353
<b>Other comprehensive income (loss)</b>				
Total net unrealized gains (losses) arising during the period	1,058,518	(1,524,166)	9,440,894	(3,436,009)
Less net realized investment gains (losses)	206,890	200,657	335,841	(18,521)
Net unrealized gains (losses)	851,628	(1,724,823)	9,105,053	(3,417,488)
Less adjustment to deferred acquisition costs	19,392	(16,661)	146,605	(34,669)
Other comprehensive income (loss) before income tax expense	832,236	(1,708,162)	8,958,448	(3,382,819)
Income tax expense (benefit)	166,449	(341,633)	1,791,689	(676,565)
<b>Total other comprehensive income (loss)</b>	665,787	(1,366,529)	7,166,759	(2,706,254)
<b>Total comprehensive income (loss)</b>	<u>\$ 1,164,373</u>	<u>\$ (718,812)</u>	<u>\$ 8,298,757</u>	<u>\$ (1,324,901)</u>

*See notes to consolidated financial statements (unaudited).*

First Trinity Financial Corporation and Subsidiaries  
Consolidated Statements of Changes in Shareholders' Equity  
Nine Months Ended September 30, 2016 and 2015  
(Unaudited)

	Common Stock \$.01 Par Value	Additional Paid-in Capital	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Accumulated Earnings	Total Shareholders' Equity
<b>Balance as of January 1, 2015</b>	\$ 80,502	\$ 28,684,748	\$ (855,304)	\$ 2,683,543	\$ 2,616,849	\$ 33,210,338
Repurchase of common stock	-	-	(38,643)	-	-	(38,643)
Stock dividend adjustment	-	(150)	-	-	150	-
Comprehensive income (loss):						
Net income	-	-	-	-	1,381,353	1,381,353
Other comprehensive loss	-	-	-	(2,706,254)	-	(2,706,254)
<b>Balance as of September 30, 2015</b>	<u>\$ 80,502</u>	<u>\$ 28,684,598</u>	<u>\$ (893,947)</u>	<u>\$ (22,711)</u>	<u>\$ 3,998,352</u>	<u>\$ 31,846,794</u>
<b>Balance as of January 1, 2016</b>	\$ 80,502	\$ 28,684,598	\$ (893,947)	\$ (2,655,817)	\$ 4,999,707	\$ 30,215,043
Comprehensive income:						
Net income	-	-	-	-	1,131,998	1,131,998
Other comprehensive income	-	-	-	7,166,759	-	7,166,759
<b>Balance as of September 30, 2016</b>	<u>\$ 80,502</u>	<u>\$ 28,684,598</u>	<u>\$ (893,947)</u>	<u>\$ 4,510,942</u>	<u>\$ 6,131,705</u>	<u>\$ 38,513,800</u>

See notes to consolidated financial statements (unaudited).

First Trinity Financial Corporation and Subsidiaries  
Consolidated Statements of Cash Flows  
(Unaudited)

	Nine Months Ended September 30,	
	2016	2015
<b>Operating activities</b>		
Net income	\$ 1,131,998	\$ 1,381,353
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for depreciation	109,587	147,462
Accretion of discount on investments	(1,278,028)	(758,333)
Net realized investment gains	(307,250)	(786,852)
Loss on other-than-temporary impairment	-	305,334
Gain on reinsurance assumption	-	(588,923)
Amortization of policy acquisition cost	1,588,938	1,285,997
Policy acquisition cost deferred	(5,142,381)	(3,819,582)
Mortgage loan origination fees deferred	(4,530)	(74,000)
Amortization of loan origination fees	54,032	51,362
Amortization of value of insurance business acquired	281,175	291,918
Provision for deferred federal income tax benefit (expense)	163,685	(157,546)
Interest credited to policyholders	5,090,162	4,052,780
Change in assets and liabilities:		
Accrued investment income	56,974	(361,106)
Policy loans	(75,655)	51,961
Short-term investments	549,850	541,655
Allowance for mortgage loan losses	36,096	48,585
Recoverable from reinsurers	(37,538)	24,609
Agents' balances and due premiums	(344,558)	(526,319)
Other assets (excludes \$470 of 2016 depreciation)	(4,042,745)	(1,078,478)
Future policy benefits	4,002,756	2,628,204
Policy claims	94,291	53,147
Other policy liabilities	5,631	(12,996)
Other liabilities	2,267,785	1,871,421
<b>Net cash provided by operating activities</b>	<b>4,200,275</b>	<b>4,571,653</b>
<b>Investing activities</b>		
Purchases of fixed maturity securities	(6,163,564)	(26,575,622)
Maturities of fixed maturity securities	4,657,000	1,634,000
Sales of fixed maturity securities	10,205,935	5,937,843
Purchases of equity securities	(14,480)	(551,229)
Sales of equity securities	128,010	533,813
Reinsurance assumption	-	64,935
Purchases of mortgage loans	(20,669,087)	(23,665,861)
Payments on mortgage loans	11,317,427	7,452,257
Purchases of other long-term investments	(11,340,463)	(11,968,198)
Payments on other long-term investments	3,114,728	3,245,071
Sale of real estate	-	7,083,246
<b>Net cash used in investing activities</b>	<b>(8,764,494)</b>	<b>(36,809,745)</b>
<b>Financing activities</b>		
Policyholders' account deposits	32,177,094	45,590,381
Policyholders' account withdrawals	(9,957,150)	(7,416,790)
Purchases of treasury stock	-	(38,643)
Repayment of notes payable	-	(4,076,473)
<b>Net cash provided by financing activities</b>	<b>22,219,944</b>	<b>34,058,475</b>
<b>Increase in cash</b>	<b>17,655,725</b>	<b>1,820,383</b>
Cash and cash equivalents, beginning of period	9,047,586	10,158,386
Cash and cash equivalents, end of period	<u>\$ 26,703,311</u>	<u>\$ 11,978,769</u>

See notes to consolidated financial statements (unaudited).

First Trinity Financial Corporation and Subsidiaries  
Consolidated Statements of Cash Flows (continued)  
Supplemental Disclosure – Cash and Non-Cash Impact on Operating, Investing and Financing Activities  
(Unaudited)

During 2016, the Company foreclosed on three residential mortgage loans of real estate totaling \$198,622 and transferred those properties to investment real estate that are now held for sale. The Company reduced the carrying value of this residential real estate obtained through foreclosure to the lower of acquisition cost or net realizable value.

In conjunction with these foreclosures, the non-cash impact on investing activities is summarized as follows:

	Nine Months Ended September 30, 2016
Reductions in mortgage loans due to foreclosure	\$ 198,622
Investment real estate held-for-sale acquired through foreclosure	(198,622)
Net cash provided (used) in investing activities	<u>\$ -</u>

On April 28, 2015, the Company acquired a block of life insurance policies and annuity contracts according to the terms of an assumption reinsurance agreement. The Company acquired assets of \$3,644,839 (including cash), assumed liabilities of \$3,055,916 and recorded a gain on reinsurance assumption of \$588,923. During third quarter 2015, the Company completed its evaluation of assets, liabilities and gain associated with the reinsurance assumption and adjusted the assets, liabilities and gain on reinsurance assumption initially estimated and recorded in second quarter 2015.

In conjunction with this 2015 reinsurance assumption transaction, the cash and non-cash impact on operating, investing and financing activities is summarized as follows:

	Nine Months Ended September 30, 2015
Cash used in reinsurance assumption	\$ -
Cash provided in reinsurance assumption	64,935
Increase in cash from reinsurance assumption	64,935
Fair value of assets acquired in reinsurance assumption (excluding cash)	
Available-for-sale fixed maturity securities	3,534,093
Policy loans	5,869
Accrued investment income	37,792
Due premiums	2,150
Total fair value of assets acquired (excluding cash)	3,579,904
Fair value of liabilities assumed in reinsurance assumption	
Policyholders' account balances	2,966,827
Future policy benefits	89,089
Total fair value of liabilities assumed	3,055,916
Fair value of net assets acquired in reinsurance assumption (excluding cash)	523,988
Fair value of net assets acquired in reinsurance assumption (including cash)	<u>\$ 588,923</u>

See notes to consolidated financial statements (unaudited).



**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**September 30, 2016**  
**(Unaudited)**

**1. Organization and Significant Accounting Policies**

***Nature of Operations***

First Trinity Financial Corporation (the “Company” or “FTFC”) is the parent holding company of Trinity Life Insurance Company (“TLIC”), Family Benefit Life Insurance Company (“FBLIC”) and First Trinity Capital Corporation (“FTCC”). The Company was incorporated in Oklahoma on April 19, 2004, for the primary purpose of organizing a life insurance subsidiary.

The Company owns 100% of TLIC. TLIC owns 100% of FBLIC. TLIC and FBLIC are primarily engaged in the business of marketing, underwriting and distributing a broad range of individual life insurance and annuity products to individuals. TLIC’s and FBLIC’s current product portfolio consists of a modified premium whole life insurance policy with a flexible premium deferred annuity rider, whole life, term, final expense, accidental death and dismemberment and annuity products. The term products are both renewable and convertible and issued for 10, 15, 20 and 30 years. They can be issued with premiums fully guaranteed for the entire term period or with a limited premium guarantee. The final expense is issued as either a simplified issue or as a graded benefit, determined by underwriting. The TLIC and FBLIC products are sold through independent agents. TLIC is licensed in the states of Illinois, Kansas, Kentucky, Nebraska, North Dakota, Ohio, Oklahoma and Texas. FBLIC is licensed in the states of Alabama, Arizona, Arkansas, Colorado, Georgia, Illinois, Indiana, Kansas, Kentucky, Louisiana, Michigan, Mississippi, Missouri, Nebraska, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, South Dakota, Tennessee, Texas, Utah, Virginia and West Virginia.

The Company owns 100% of FTCC that was incorporated in 2006, and began operations in January 2007. FTCC provided financing for casualty insurance premiums for individuals and companies and was licensed to conduct premium financing business in the states of Alabama, Arkansas, Louisiana, Mississippi and Oklahoma. FTCC currently has no operations other than minor premium refunds, collections of past due accounts and accounts involved in litigation.

***Company Capitalization***

The Company raised \$1,450,000 from two private placement stock offerings during 2004 and \$25,669,480 from two public stock offerings and one private placement stock offering from June 22, 2005 through February 23, 2007; June 29, 2010 through April 30, 2012 and August 15, 2012 through March 8, 2013. The Company issued 7,347,488 shares of its common stock and incurred \$3,624,518 of offering costs during these private placements and public stock offerings.

The Company also issued 702,685 shares of its common stock in connection with two stock dividends paid to shareholders in 2011 and 2012 that resulted in accumulated earnings being charged \$5,270,138 with an offsetting credit of \$5,270,138 to common stock and additional paid-in capital.

The Company has also purchased 247,580 shares of treasury stock at a cost of \$893,947 from former members of the Board of Directors including the former Chairman of the Board of Directors, a former agent, the former spouse of the Company’s Chairman, Chief Executive Officer and President and a charitable organization where a former member of the Board of Directors had donated shares of the Company’s common stock.

***Acquisition of Other Companies***

On December 23, 2008, FTFC acquired 100% of the outstanding common stock of First Life America Corporation (“FLAC”) from an unaffiliated company. The acquisition of FLAC was accounted for as a purchase. The aggregate purchase price for FLAC was approximately \$2,695,000 (including direct cost associated with the acquisition of approximately \$195,000). The acquisition of FLAC was financed with the working capital of FTFC.

On December 31, 2008, FTFC made FLAC a 15 year loan in the form of a surplus note in the amount of \$250,000 with an interest rate of 6% payable monthly, that was approved by the Oklahoma Insurance Department (“OID”). This surplus note is eliminated in consolidation.

**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**September 30, 2016**  
**(Unaudited)**

**1. Organization and Significant Accounting Policies (continued)**

On August 31, 2009, two of the Company's subsidiaries, Trinity Life Insurance Company ("Old TLIC") and FLAC, were merged, with FLAC being the surviving company. Immediately following the merger, FLAC changed its name to TLIC.

On December 28, 2011, TLIC acquired 100% of the outstanding common stock of FBLIC from FBLIC's shareholders. The acquisition of FBLIC was accounted for as a purchase. The aggregate purchase price for the acquisition of FBLIC was \$13,855,129. The acquisition of FBLIC was financed with the working capital of TLIC.

On April 28, 2015, the Company acquired a block of life insurance policies and annuity contracts according to the terms of an assumption reinsurance agreement. The Company acquired assets of \$3,644,839 (including cash), assumed liabilities of \$3,055,916 and recorded a gain on reinsurance assumption of \$588,923. During third quarter 2015, the Company completed its evaluation of assets, liabilities and gain associated with the reinsurance assumption and adjusted the assets, liabilities and gain on reinsurance assumption initially estimated and recorded in second quarter 2015.

***Basis of Presentation***

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting primarily of normal recurring accruals) considered necessary for a fair presentation of the results for the interim periods have been included.

The results of operations for the three and nine months ended September 30, 2016 are not necessarily indicative of the results to be expected for the year ended December 31, 2016 or for any other interim period or for any other future year. Certain financial information which is normally included in notes to consolidated financial statements prepared in accordance with U.S. GAAP, but which is not required for interim reporting purposes, has been condensed or omitted. The accompanying consolidated financial statements and notes thereto should be read in conjunction with the financial statements and notes thereto included in the Company's report on Form 10-K for the year ended December 31, 2015.

***Principles of Consolidation***

The consolidated financial statements include the accounts and operations of the Company and its subsidiaries. All intercompany accounts and transactions are eliminated in consolidation.

***Reclassifications***

Certain reclassifications have been made in the prior year and prior quarter financial statements to conform to current year and current quarter classifications. These reclassifications had no effect on previously reported net income or shareholders' equity.

***Use of Estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Although these estimates are based on management's knowledge of current events and actions it may undertake in the future, they may ultimately differ from actual results.

***Common Stock***

Common stock is fully paid, non-assessable and has a par value of \$.01 per share.

**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**September 30, 2016**  
**(Unaudited)**

**1. Organization and Significant Accounting Policies (continued)**

***Treasury Stock***

Treasury stock, representing shares of the Company's common stock that have been reacquired after having been issued and fully paid, is recorded at the reacquisition cost and the shares are no longer outstanding.

***Subsequent Events***

Management has evaluated all events subsequent to September 30, 2016 through the date that these financial statements have been issued.

***Recent Accounting Pronouncements***

***Revenue from Contracts with Customers***

In May 2014, the Financial Accounting Standards Board ("FASB") issued updated guidance to clarify the principles for recognizing revenue. While insurance contracts are not within the scope of this updated guidance, the Company's fee income related to providing services will be subject to this updated guidance. The updated guidance requires an entity to recognize revenue as performance obligations are met, in order to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration the entity is entitled to receive for those goods or services.

The following steps are applied in the updated guidance: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract and (5) recognize revenue when, or as, the entity satisfies a performance obligation.

In July 2015, the FASB deferred the effective date of the updated guidance on revenue recognition by one year to the quarter ending March 31, 2018. The adoption of this guidance is not expected to have a material effect on the Company's result of operations, financial position or liquidity.

***Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period***

In June 2014, the FASB issued updated guidance to resolve diversity in practice concerning employee share-based payments that contain performance targets that could be achieved after the requisite service period. Many reporting entities account for performance targets that could be achieved after the requisite service period as performance conditions that affect the vesting of the award and, therefore, do not reflect the performance targets in the estimate of the grant-date fair value of the award. Other reporting entities treat those performance targets as nonvesting conditions that affect the grant-date fair value of the award.

The updated guidance requires that a performance target that affects vesting and that can be achieved after the requisite service period be treated as a performance condition. As such, the performance target that affects vesting should not be reflected in estimating that fair value of the award at the grant date. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the periods for which service has been rendered. If the performance target becomes probable of being achieved before the end of the service period, the remaining unrecognized compensation cost for which requisite service has not yet been rendered is recognized prospectively over the remaining service period. The total amount of compensation cost recognized during and after the service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest.

**First Trinity Financial Corporation and Subsidiaries**  
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**1. Organization and Significant Accounting Policies (continued)**

The updated guidance is effective for annual and interim periods beginning after December 15, 2015, with early adoption permitted. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

*Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*

In August 2014, the FASB issued guidance to address the diversity in practice in determining when there is substantial doubt about an entity's ability to continue as a going concern and when an entity must disclose certain relevant conditions and events. The new guidance requires an entity to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued). The new guidance allows the entity to consider the mitigating effects of management's plans that will alleviate the substantial doubt and requires certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans.

If conditions or events raise substantial doubt that is not alleviated, an entity should disclose that there is substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued), along with the principal conditions or events that raise substantial doubt, management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations and management's plans that are intended to mitigate those conditions.

The guidance is effective for annual periods ending after December 15, 2016, and interim and annual periods thereafter. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

*Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity*

In November 2014, the FASB issued updated guidance to clarify when the separation of certain embedded derivative features in a hybrid financial instrument that is issued in the form of a share is required. That is, an entity will continue to evaluate whether the economic characteristics and risks of the embedded derivative feature are clearly and closely related to those of the host contract. Specifically, the amendments clarify that an entity should consider all relevant terms and features, including the embedded derivative feature being evaluated for bifurcation, in evaluating the nature of the host contract.

Furthermore, the amendments clarify that no single term or feature would necessarily determine the economic characteristics and risks of the host contract. Rather, the nature of the host contract depends upon the economic characteristics and risks of the entire hybrid financial instrument.

The updated guidance is effective for reporting periods beginning after December 15, 2015. Early adoption is permitted. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

*Troubled Debt Restructurings by Creditors*

In January 2015, the FASB issued updated guidance for troubled debt restructurings clarifying when an in substance repossession or foreclosure occurs, and when a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan. The new guidance is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2015. This guidance can be elected for prospective adoption or by using a retrospective transition method. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

**First Trinity Financial Corporation and Subsidiaries**  
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**1. Organization and Significant Accounting Policies (continued)**

*Amendments to the Consolidation Analysis*

In February 2015, the FASB issued updated guidance that makes targeted amendments to the current consolidation accounting guidance. The update is in response to accounting complexity concerns, particularly from the asset management industry. The guidance simplifies consolidation accounting by reducing the number of approaches to consolidation, provides a scope exception to registered money market funds and similar unregistered money market funds and ends the indefinite deferral granted to investment companies from applying the variable interest entity guidance.

The updated guidance is effective for annual and interim periods beginning after December 15, 2015. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

*Simplifying the Presentation of Debt Issuance Costs*

In April 2015, the FASB issued updated guidance to clarify the required presentation of debt issuance costs. The amended guidance requires that debt issuance costs be presented in the balance sheet as a direct reduction from the carrying amount of the recognized debt liability, consistent with the treatment of debt discounts. Amortization of debt issuance costs is to be reported as interest expense. The recognition and measurement guidance for debt issuance costs are not affected by the updated guidance. The updated guidance is effective for reporting periods beginning after December 15, 2015. Early adoption is permitted. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

*Simplifying the Accounting for Measurement-Period Adjustments*

In September 2015, the FASB issued updated guidance regarding business combinations that requires an acquirer to recognize post-close measurement adjustments for provisional amounts in the period the adjustment amounts are determined rather than retrospectively. The acquirer is also required to recognize, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the provisional amount, calculated as if the accounting had been completed at the acquisition date. The updated guidance is to be applied prospectively effective for annual and interim periods beginning after December 15, 2015. In connection with business combinations which have already been completed, the adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

*Recognition and Measurement of Financial Assets and Financial Liabilities*

In January 2016, the FASB issued updated guidance regarding financial instruments. This guidance intends to enhance reporting for financial instruments and addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The significant amendments in this update generally require equity investments to be measured at fair value with changes in fair value recognized in net income, require the use of an exit price notion when measuring the fair value of financial instruments for disclosure purposes and clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities. This guidance also intends to enhance the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments.

This guidance is effective for fiscal years beginning after December 15, 2017. The recognition and measurement provisions of this guidance will be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption and early adoption is not permitted. The Company is evaluating this guidance but expects the primary impact will be the recognition of unrealized gains and losses on available-for-sale equity securities in net income. Currently, all unrealized gains and losses on available-for-sale equity securities are recognized in other comprehensive income (loss).

**First Trinity Financial Corporation and Subsidiaries**  
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**1. Organization and Significant Accounting Policies (continued)**

The effect of the adoption of this guidance on the Company's results of operations, financial position and liquidity is primarily dependent on the fair value of the available-for-sale equity securities in future periods and the existence of a deferred tax asset related to available-for-sale securities in future periods that have not yet been fully assessed.

*Leases*

In February 2016, the FASB issued updated guidance to require lessees to recognize a right-to-use asset and a lease liability for leases with terms of more than 12 months. The updated guidance retains the two classifications of a lease as either an operating or finance lease (previously referred to as a capital lease). Both lease classifications require the lessee to record the right-to-use asset and the lease liability based upon the present value of cash flows. Finance leases will reflect the financial arrangement by recognizing interest expense on the lease liability separately from the amortization expense of the right-to-use asset. Operating leases will recognize lease expense (with no separate recognition of interest expense) on a straight-line basis over the term of the lease. The accounting by lessors is not significantly changed by the updated guidance. The updated guidance requires expanded qualitative and quantitative disclosures, including additional information about the amounts recorded in the financial statements.

The updated guidance is effective for reporting periods beginning after December 15, 2018, and will require that the earliest comparative period presented include the measurement and recognition of existing leases with an adjustment to equity as if the updated guidance had always been applied. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

*Improvements to Employee Share-Based Payment Accounting*

In March 2016, the FASB issued updated guidance to simplify several aspects of accounting for share-based payment transactions as follows:

Accounting for Income Taxes

Under current accounting guidance, if the deduction for a share-based payment award for tax purposes exceeds, or is less than, the compensation cost recognized for financial reporting purposes, the resulting excess tax benefit, or tax deficiency, is reported as part of additional paid-in capital. Under the updated guidance, these excess tax benefits, or tax deficiencies, are reported as part of income tax expense or benefit in the income statement. The updated guidance also removes the requirement to delay recognition of any excess tax benefit when there are no current taxes payable to which the benefit would be applied. The tax-related cash flows resulting from share-based payments are to be included with other income tax cash flows as an operating activity rather than being reported separately as a financing activity.

Forfeitures

The updated guidance permits an entity to make an accounting policy election to either account for forfeitures when they occur or continue to apply the current method of accruing the compensation cost based on the number of awards that are expected to vest.

Minimum Statutory Tax Withholding Requirements

The updated guidance changes the threshold amount an entity can withhold for taxes when settling an equity award and still qualify for equity classification. A company can withhold up to the maximum statutory tax rates in the employees' applicable jurisdiction rather than withholding up to the employers' minimum statutory withholding requirement. The update also clarifies that all cash payments made to taxing authorities on behalf of employees for withheld shares are to be presented in financing activities on the statement of cash flows.

**First Trinity Financial Corporation and Subsidiaries**  
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**1. Organization and Significant Accounting Policies (continued)**

Transition

The updated guidance is effective for reporting periods beginning after December 15, 2016. Early adoption is permitted in any interim period; if early adoption is elected, the entity must adopt all of the amendments in the same reporting period and reflect any adjustments as of the beginning of the fiscal year. The Company has not elected early adoption. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

*Simplifying the Transition to the Equity Method of Accounting*

In March 2016, the FASB issued updated guidance that eliminates the requirement to retroactively apply the equity method of accounting when an investment that was previously accounted for using another method of accounting becomes qualified to apply the equity method due to an increase in the level of ownership interest or degree of influence. If the investment was previously accounted for as an available-for-sale security, any related unrealized gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for the equity method is recognized through earnings. The updated guidance is effective for reporting periods beginning after December 15, 2016, and is to be applied prospectively. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

*Contingent Put and Call Options in Debt Instruments*

In March 2016, the FASB issued updated guidance clarifying that when a call (put) option in a debt instrument can accelerate the repayment of principal on the debt instrument, a reporting entity does not need to assess whether the contingent event that triggers the ability to exercise the call (put) option is related to interest rates or credit risk in determining whether the option should be accounted for separately. The updated guidance is effective for reporting periods beginning after December 15, 2016. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

*Measurement of Credit Losses on Financial Instruments*

In June 2016, the FASB issued updated guidance for the accounting for credit losses for financial instruments. The updated guidance applies a new credit loss model (current expected credit losses or CECL) for determining credit-related impairments for financial instruments measured at amortized cost (e.g. reinsurance recoverables) and requires an entity to estimate the credit losses expected over the life of an exposure or pool of exposures. The estimate of expected credit losses should consider historical information, current information, as well as reasonable and supportable forecasts, including estimates of prepayments. The expected credit losses, and subsequent adjustments to such losses, will be recorded through an allowance account that is deducted from the amortized cost basis of the financial asset, with the net carrying value of the financial asset presented on the consolidated balance sheet at the amount expected to be collected.

The updated guidance also amends the current other-than-temporary impairment model for available-for-sale debt securities by requiring the recognition of impairments relating to credit losses through an allowance account and limits the amount of credit loss to the difference between a security's amortized cost basis and its fair value. In addition, the length of time a security has been in an unrealized loss position will no longer impact the determination of whether a credit loss exists.

The updated guidance is effective for reporting periods beginning after December 15, 2019. Early adoption is permitted for reporting periods beginning after December 15, 2018. The Company will not be able to determine the impact that the updated guidance will have on its results of operations, financial position or liquidity until the updated guidance is adopted.

**First Trinity Financial Corporation and Subsidiaries**  
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**(Unaudited)**

**1. Organization and Significant Accounting Policies** (continued)

*Classification of Certain Cash Receipts and Cash Payment*

In August 2016, the FASB issued new guidance that clarifies the classification of certain cash receipts and cash payments in the statement of cash flows under eight different scenarios including, but not limited to: (i) debt prepayment or debt extinguishment costs; (ii) proceeds from the settlement of corporate-owned life insurance policies including bank-owned life insurance policies; (iii) distributions received from equity method investees; and (iv) separately identifiable cash flows and application of the predominance principle. This guidance is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the impact of this guidance on its statement of cash flows.



**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
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**(Unaudited)**

**2. Investments**

***Fixed Maturity and Equity Securities Available-For-Sale***

Investments in fixed maturity and equity securities available-for-sale as of September 30, 2016 and December 31, 2015 are summarized as follows:

	Amortized Cost or Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	September 30, 2016 (Unaudited)			
Fixed maturity securities				
U.S. government and U.S. government agencies	\$ 3,095,489	\$ 123,863	\$ 7,868	\$ 3,211,484
States and political subdivisions	8,940,717	530,240	-	9,470,957
Residential mortgage-backed securities	36,554	44,073	-	80,627
Corporate bonds	101,538,123	5,331,077	1,041,809	105,827,391
Foreign bonds	15,375,464	817,184	191,046	16,001,602
Total fixed maturity securities	128,986,347	6,846,437	1,240,723	134,592,061
Equity securities				
Mutual funds	342,519	1,952	-	344,471
Corporate preferred stock	149,725	8,275	-	158,000
Corporate common stock	191,684	119,269	-	310,953
Total equity securities	683,928	129,496	-	813,424
Total fixed maturity and equity securities	<u>\$ 129,670,275</u>	<u>\$ 6,975,933</u>	<u>\$ 1,240,723</u>	<u>\$ 135,405,485</u>
	December 31, 2015			
Fixed maturity securities				
U.S. government and U.S. government agencies	\$ 2,793,161	\$ 136,190	\$ 108,597	\$ 2,820,754
States and political subdivisions	8,993,848	61,592	102,835	8,952,605
Residential mortgage-backed securities	49,980	43,846	-	93,826
Corporate bonds	109,164,942	1,820,894	4,234,897	106,750,939
Foreign bonds	17,026,524	185,225	1,273,846	15,937,903
Total fixed maturity securities	138,028,455	2,247,747	5,720,175	134,556,027
Equity securities				
Mutual funds	335,554	-	10,613	324,941
Corporate preferred stock	259,993	6,035	990	265,038
Corporate common stock	194,668	117,196	9,043	302,821
Total equity securities	790,215	123,231	20,646	892,800
Total fixed maturity and equity securities	<u>\$ 138,818,670</u>	<u>\$ 2,370,978</u>	<u>\$ 5,740,821</u>	<u>\$ 135,448,827</u>

**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
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**(Unaudited)**

**2. Investments (continued)**

All securities in an unrealized loss position as of the financial statement dates, the estimated fair value, pre-tax gross unrealized loss and number of securities by length of time that those securities have been continuously in an unrealized loss position as of September 30, 2016 and December 31, 2015 are summarized as follows:

	Fair Value	Unrealized Loss	Number of Securities
	September 30, 2016 (Unaudited)		
Fixed maturity securities			
Less than 12 months			
U.S. government and U.S. government agencies	\$ 1,241,573	\$ 7,868	3
Corporate bonds	5,129,945	130,041	18
Foreign bonds	296,583	2,610	1
Total less than 12 months	6,668,101	140,519	22
More than 12 months			
Corporate bonds	8,599,757	911,768	39
Foreign bonds	2,659,276	188,436	13
Total more than 12 months	11,259,033	1,100,204	52
Total fixed maturity securities	<u>\$ 17,927,134</u>	<u>\$ 1,240,723</u>	<u>74</u>
	December 31, 2015		
Fixed maturity securities			
Less than 12 months			
U.S. government and U.S. government agencies	\$ 381,592	\$ 20,006	2
States and political subdivisions	5,422,934	102,835	26
Corporate bonds	46,907,532	2,646,997	186
Foreign bonds	9,155,830	879,659	40
Total less than 12 months	61,867,888	3,649,497	254
More than 12 months			
U.S. government and U.S. government agencies	1,041,409	88,591	2
Corporate bonds	5,646,642	1,587,900	31
Foreign bonds	489,008	394,187	3
Total more than 12 months	7,177,059	2,070,678	36
Total fixed maturity securities	69,044,947	5,720,175	290
Equity securities			
Less than 12 months			
Mutual funds	74,547	10,613	1
Corporate preferred stock	109,279	990	1
Corporate common stock	41,804	9,043	1
Total equity securities	225,630	20,646	3
Total fixed maturity and equity securities	<u>\$ 69,270,577</u>	<u>\$ 5,740,821</u>	<u>293</u>

As of September 30, 2016, the Company held 74 available-for-sale fixed maturity securities with an unrealized loss of \$1,240,723, fair value of \$17,927,134 and amortized cost of \$19,167,857. The ratio of the fair value to the amortized cost of these 74 securities is 94%.

As of December 31, 2015, the Company held 290 available-for-sale fixed maturity securities with an unrealized loss of \$5,720,175, fair value of \$69,044,947 and amortized cost of \$74,765,122. These unrealized losses were primarily due to market interest rate movements in the bond market as of December 31, 2015 coupled with a downturn in the Chinese economy, decreases in the value of commodities and a drop in oil prices. The ratio of the fair value to the amortized cost of these 290 securities is 92%.

**First Trinity Financial Corporation and Subsidiaries**  
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**2. Investments** (continued)

As of September 30, 2016, the Company had no equity security with an unrealized loss.

As of December 31, 2015, the Company had three available-for-sale equity securities with an unrealized loss of \$20,646, fair value of \$225,630 and cost of \$246,276. The ratio of fair value to cost of these securities is 92%.

Fixed maturity securities were 92% and 94% investment grade as rated by Standard & Poor's as of September 30, 2016 and December 31, 2015, respectively.

The Company's decision to record an impairment loss is primarily based on whether the security's fair value is likely to remain significantly below its book value based on all of the factors considered. Factors that are considered include the length of time the security's fair value has been below its carrying amount, the severity of the decline in value, the credit worthiness of the issuer and the coupon and/or dividend payment history of the issuer. The Company also assesses whether it intends to sell or whether it is more likely than not that it may be required to sell the security prior to its recovery in value.

For any fixed maturity securities that are other-than-temporarily impaired, the Company determines the portion of the other-than-temporary impairment that is credit-related and the portion that is related to other factors. The credit-related portion is the difference between the expected future cash flows and the amortized cost basis of the fixed maturity security, and that difference is charged to earnings. The non-credit-related portion representing the remaining difference to fair value is recognized in other comprehensive income (loss). Only in the case of a credit-related impairment where management has the intent to sell the security, or it is more likely than not that it will be required to sell the security before recovery of its cost basis, is a fixed maturity security adjusted to fair value and the resulting losses recognized in realized gains (losses) in the consolidated statements of operations. Any other-than-temporary impairments on equity securities are recorded in the consolidated statements of operations in the periods incurred as the difference between fair value and cost.

There were no impairments during the nine months ended September 30, 2016.

During second quarter and fourth quarter 2015, the Company impaired its bonds in a mining corporation with a total par value of \$600,000 as a result of an analysis of the mining corporation's ability to fulfill its obligations. This impairment was considered fully credit-related, resulting in a charge to the statement of operations before tax of \$304,256 and \$502,013 for the six months ended June 30, 2015 and year ended December 31, 2015, respectively. This charge represents the credit-related portion of the difference between the amortized cost basis of the security and its fair value. The Company experienced no additional other-than-temporary impairments during 2015.

Management believes that the Company will fully recover its cost basis in the securities held as of September 30, 2016, and management does not have the intent to sell nor is it more likely than not that the Company will be required to sell such securities until they recover or mature. The remaining temporary impairments shown herein are primarily the result of the current interest rate environment rather than credit factors that would imply other-than-temporary impairment.

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**2. Investments (continued)**

Net unrealized gains (losses) included in other comprehensive income (loss) for investments classified as available-for-sale, net of the effect of deferred income taxes and deferred acquisition costs assuming that the appreciation (depreciation) had been realized as of September 30, 2016 and December 31, 2015, are summarized as follows:

	(Unaudited)	
	<u>September 30, 2016</u>	<u>December 31, 2015</u>
Unrealized appreciation (depreciation)		
on available-for-sale securities	\$ 5,735,210	\$ (3,369,843)
Adjustment to deferred acquisition costs	(96,532)	50,073
Deferred income taxes	<u>(1,127,736)</u>	<u>663,953</u>
Net unrealized appreciation (depreciation)		
on available-for-sale securities	<u>\$ 4,510,942</u>	<u>\$ (2,655,817)</u>

The Company's investment in lottery prize cash flows categorized as other long-term investments in the statement of financial position was \$41,658,491 and \$31,566,927 as of September 30, 2016 and December 31, 2015, respectively. The lottery prize cash flows are assignments of the future rights from lottery winners purchased at a discounted price. Payments on these investments are made by state run lotteries.

The amortized cost and fair value of fixed maturity available-for-sale securities and other long-term investments as of September 30, 2016, by contractual maturity, are summarized as follows:

	September 30, 2016 (Unaudited)			
	<u>Fixed Maturity Available-For-Sale Securities</u>		<u>Other Long-Term Investments</u>	
	<u>Amortized Cost</u>	<u>Fair Value</u>	<u>Amortized Cost</u>	<u>Fair Value</u>
Due in one year or less	\$ 7,796,909	\$ 7,872,902	\$ 5,309,897	\$ 5,381,733
Due in one year through five years	32,037,852	33,262,422	15,581,268	17,021,625
Due after five years through ten years	44,835,640	46,380,935	11,549,032	14,358,534
Due after ten years	44,279,392	46,995,175	9,218,294	15,656,812
Due at multiple maturity dates	<u>36,554</u>	<u>80,627</u>	<u>-</u>	<u>-</u>
	<u>\$ 128,986,347</u>	<u>\$ 134,592,061</u>	<u>\$ 41,658,491</u>	<u>\$ 52,418,704</u>

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.

**First Trinity Financial Corporation and Subsidiaries**  
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**(Unaudited)**

**2. Investments (continued)**

Proceeds and gross realized gains (losses) from the sales, calls and maturities of fixed maturity securities available-for-sale, equity securities available-for-sale, mortgage loans on real estate and investment real estate for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

	Fixed Maturity Securities		Equity Securities		Mortgage Loans on Real Estate		Investment Real Estate	
	2016	2015	2016	2015	2016	2015	2016	2015
Three Months Ended September 30, (Unaudited)								
Proceeds	\$ 7,368,724	\$ 4,983,682	\$ -	\$ -	\$ 7,655,905	\$ 3,328,222	\$ -	\$ -
Gross realized gains	242,910	225,058	-	-	-	79,028	-	-
Gross realized losses	(36,020)	(23,323)	-	-	(46,582)	-	-	-
Loss on other-than-temporary impairment	-	(1,078)	-	-	-	-	-	-
Nine Months Ended September 30, (Unaudited)								
Proceeds	\$14,862,935	\$ 7,571,843	\$ 128,010	\$ 533,813	\$11,317,427	\$ 7,452,257	\$ -	\$ 7,083,246
Gross realized gains	405,960	313,690	8,711	996	-	109,837	-	390,202
Gross realized losses	(77,362)	(24,977)	(1,468)	(2,896)	(28,591)	-	-	-
Loss on other-than-temporary impairment	-	(305,334)	-	-	-	-	-	-

The accumulated change in net unrealized investment gains (losses) for fixed maturity and equity securities available-for-sale for the three and nine months ended September 30, 2016 and 2015 and the amount of realized investment gains on fixed maturity securities available-for-sale, equity securities available-for-sale, mortgage loans on real estate and investment real estate for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

	Three Months Ended September 30, (Unaudited)		Nine Months Ended September 30, (Unaudited)	
	2016	2015	2016	2015
Change in unrealized investment gains:				
Available-for-sale securities:				
Fixed maturity securities	\$ 817,963	\$ (1,689,567)	\$ 9,078,142	\$ (3,345,103)
Equity securities	33,665	(35,256)	26,911	(72,385)
Net realized investment gains (losses):				
Available-for-sale securities:				
Fixed maturity securities	206,890	200,657	328,598	(16,621)
Equity securities	-	-	7,243	(1,900)
Mortgage loans on real estate	(46,582)	79,028	(28,591)	109,837
Investment real estate	-	-	-	390,202

**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
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**2. Investments (continued)**

Major categories of net investment income for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

	Three Months Ended September 30, (Unaudited)		Nine Months Ended September 30, (Unaudited)	
	2016	2015	2016	2015
Fixed maturity securities	\$ 1,435,041	\$ 1,400,291	\$ 4,535,560	\$ 3,819,806
Equity securities	6,728	8,797	20,568	29,051
Other long-term investments	687,042	501,221	1,857,366	1,340,050
Mortgage loans	1,417,445	1,172,040	4,098,943	3,108,912
Policy loans	27,348	25,248	79,937	75,554
Real estate	62,391	97,657	246,327	357,067
Short-term and other investments	56,806	46,018	198,950	159,644
Gross investment income	3,692,801	3,251,272	11,037,651	8,890,084
Investment expenses	(388,821)	(334,955)	(1,114,834)	(1,061,445)
Net investment income	\$ 3,303,980	\$ 2,916,317	\$ 9,922,817	\$ 7,828,639

TLIC and FBLIC are required to hold assets on deposit with various state insurance departments for the benefit of policyholders and other special deposits in accordance with statutory rules and regulations. As of September 30, 2016 and December 31, 2015, these required deposits, included in investment assets, had amortized costs that totaled \$4,087,455 and \$3,989,742, respectively. As of September 30, 2016 and December 31, 2015, these required deposits had fair values that totaled \$4,244,136 and \$4,034,042, respectively.

The Company's mortgage loans by property type as of September 30, 2016 and December 31, 2015 are summarized as follows:

	(Unaudited)			
	September 30, 2016		December 31, 2015	
	Amount	Percentage	Amount	Percentage
Commercial mortgage loans				
Retail stores	\$ 1,094,697	1.61%	\$ 1,272,881	2.17%
Office buildings	183,383	0.27%	191,774	0.32%
Total commercial mortgage loans	1,278,080	1.88%	1,464,655	2.49%
Residential mortgage loans	66,619,223	98.12%	57,310,263	97.51%
Total mortgage loans	\$ 67,897,303	100.00%	\$ 58,774,918	100.00%

**First Trinity Financial Corporation and Subsidiaries**  
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**2. Investments (continued)**

The Company's investment real estate as of September 30, 2016 and December 31, 2015 is summarized as follows:

	(Unaudited)	
	<u>September 30, 2016</u>	<u>December 31, 2015</u>
Land - held for the production of income	\$ 213,160	\$ 213,160
Land - held for sale	<u>750,047</u>	<u>750,047</u>
Total land	963,207	963,207
Building - held for the production of income	2,267,557	2,267,557
Less - accumulated depreciation	<u>(1,013,323)</u>	<u>(904,206)</u>
Buildings net of accumulated depreciation	1,254,234	1,363,351
Residential real estate - held for sale	<u>198,622</u>	<u>-</u>
Total residential real estate	<u>198,622</u>	<u>-</u>
Investment real estate, net of accumulated depreciation	<u><u>\$ 2,416,063</u></u>	<u><u>\$ 2,326,558</u></u>

During 2016, the Company foreclosed on three residential mortgage loans on real estate totaling \$198,622 and transferred those properties to investment real estate that are now held for sale. The Company reduced the carrying value of this residential real estate obtained through foreclosure to the lower of acquisition cost or net realizable value.

TLIC owns approximately six and one-half acres of land located in Topeka, Kansas that includes a 20,000 square foot office building on approximately one-fourth of this land. This building and one and one-half acres of land is held for the production of income. The remaining five acres of land are held for sale. In addition, FBLIC owns one-half acre of undeveloped land located in Jefferson City, Missouri. This land is held for sale.

On March 11, 2015, the Company sold its investment real estate in buildings and land held for sale in Greensburg, Indiana; Norman, Oklahoma; Houston, Texas and Harrisonville, Missouri acquired during December 2013 and February 2014 with an aggregate carrying value of \$6,693,044 as of March 11, 2015. The Company recorded a gross profit on these sales of \$390,202 based on an aggregate sales price of \$7,083,246 less closing costs and expenses of \$20,119.

In addition, simultaneously with these sales, the Company settled its two notes payable to Grand Bank (the creditor) originated in March 2014 aggregating \$4,076,473. These loans were collateralized by the held for sale buildings and land (including assignment of the tenant leases). In connection with the repayments of the two notes payable, the Company expensed the loan origination fees remaining as of March 11, 2015 of \$72,744. During the period from January 1, 2015 to March 11, 2015, the Company incurred interest expense of \$35,181 on the two notes payable and amortized \$7,423 of loan origination fees.

**3. Fair Value Measurements**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) on the measurement date. The Company also considers the impact on fair value of a significant decrease in volume and level of activity for an asset or liability when compared with normal activity.

The Company holds fixed maturity and equity securities that are measured and reported at fair market value on the statement of financial position. The Company determines the fair market values of its financial instruments based on the fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value, as follows:

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**3. Fair Value Measurements (continued)**

Level 1 - Quoted prices in active markets for identical assets or liabilities. The Company's Level 1 assets include equity securities that are traded in an active exchange market.

Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. The Company's Level 2 assets and liabilities include fixed maturity securities with quoted prices that are traded less frequently than exchange-traded instruments or assets and liabilities whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data. This category generally includes U.S. Government and agency mortgage-backed debt securities and corporate debt securities.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. The Company's Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category generally includes certain private equity investments where independent pricing information was not able to be obtained for a significant portion of the underlying assets.

The Company has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into the three-level fair value hierarchy. If the inputs used to measure the financial instruments fall within different levels of the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument.

A review of fair value hierarchy classifications is conducted on a quarterly basis. Changes in the valuation inputs, or their ability to be observed, may result in a reclassification for certain financial assets or liabilities. Reclassifications impacting Level 3 of the fair value hierarchy are reported as transfers in and out of the Level 3 category as of the beginning of the period in which the reclassifications occur.



**First Trinity Financial Corporation and Subsidiaries**  
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**3. Fair Value Measurements** (continued)

The Company's fair value hierarchy for those financial instruments measured at fair value on a recurring basis as of September 30, 2016 and December 31, 2015 is summarized as follows:

	Level 1	Level 2	Level 3	Total
	September 30, 2016 (Unaudited)			
Fixed maturity securities, available-for-sale				
U.S. government and U.S. government agencies	\$ -	\$ 3,211,484	\$ -	\$ 3,211,484
States and political subdivisions	-	9,470,957	-	9,470,957
Residential mortgage-backed securities	-	80,627	-	80,627
Corporate bonds	-	105,827,391	-	105,827,391
Foreign bonds	-	16,001,602	-	16,001,602
Total fixed maturity securities	<u>\$ -</u>	<u>\$ 134,592,061</u>	<u>\$ -</u>	<u>\$ 134,592,061</u>
Equity securities, available-for-sale				
Mutual funds	\$ -	\$ 344,471	\$ -	\$ 344,471
Corporate preferred stock	104,720	53,280	-	158,000
Corporate common stock	264,453	-	46,500	310,953
Total equity securities	<u>\$ 369,173</u>	<u>\$ 397,751</u>	<u>\$ 46,500</u>	<u>\$ 813,424</u>
	December 31, 2015			
Fixed maturity securities, available-for-sale				
U.S. government and U.S. government agencies	\$ -	\$ 2,820,754	\$ -	\$ 2,820,754
States and political subdivisions	-	8,952,605	-	8,952,605
Residential mortgage-backed securities	-	93,826	-	93,826
Corporate bonds	-	106,750,939	-	106,750,939
Foreign bonds	-	15,937,903	-	15,937,903
Total fixed maturity securities	<u>\$ -</u>	<u>\$ 134,556,027</u>	<u>\$ -</u>	<u>\$ 134,556,027</u>
Equity securities, available-for-sale				
Mutual funds	\$ -	\$ 324,941	\$ -	\$ 324,941
Corporate preferred stock	211,278	53,760	-	265,038
Corporate common stock	256,321	-	46,500	302,821
Total equity securities	<u>\$ 467,599</u>	<u>\$ 378,701</u>	<u>\$ 46,500</u>	<u>\$ 892,800</u>

As of both September 30, 2016 and December 31, 2015, Level 3 financial instruments consisted of two private placement common stocks that have no active trading.

These private placement stocks represent investments in small financial holding companies. The fair value for these securities was determined through the use of unobservable assumptions about market participants. The Company has assumed a willing market participant would purchase the securities for the same price as the Company paid until such time as the financial holding company commences operations.

**First Trinity Financial Corporation and Subsidiaries**  
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**3. Fair Value Measurements** (continued)

Fair values for Level 1 and Level 2 assets for the Company's fixed maturity and equity securities available-for-sale are primarily based on prices supplied by a third party investment service. The third party investment service provides quoted prices in the market which use observable inputs in developing such rates.

The Company analyzes market valuations received to verify reasonableness and to understand the key assumptions used and the sources. Since the fixed maturity securities owned by the Company do not trade on a daily basis, the third party investment service prepares estimates of fair value measurements using relevant market data, benchmark curves, sector groupings and matrix pricing. As the fair value estimates of the Company's fixed maturity securities are based on observable market information rather than market quotes, the estimates of fair value on these fixed maturity securities are included in Level 2 of the hierarchy. The Company's Level 2 investments include obligations of U.S. government, U.S. government agencies, states and political subdivisions, mortgage-backed securities, corporate bonds and foreign bonds.

The Company's equity securities are included in Level 1 and Level 2 and the private placement common stocks are included in Level 3. Level 1 for those equity securities classified as such is appropriate since they trade on a daily basis, are based on quoted market prices in active markets and are based upon unadjusted prices. Level 2 for those equity securities classified as such is appropriate since they are not actively traded as of the measurement dates.

The Company's fixed maturity and equity securities available-for-sale portfolio is highly liquid and allows for a high percentage of the portfolio to be priced through pricing services.

**First Trinity Financial Corporation and Subsidiaries**  
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**3. Fair Value Measurements** (continued)

The carrying amount and fair value of the Company's financial assets and financial liabilities disclosed, but not carried, at fair value as of September 30, 2016 and December 31, 2015, and the level within the fair value hierarchy at which such assets and liabilities are measured on a recurring basis are summarized as follows:

Financial Instruments Disclosed, But Not Carried, at Fair Value:

	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
September 30, 2016 (Unaudited)					
Financial assets					
Mortgage loans on real estate					
Commercial	\$ 1,278,080	\$ 1,293,484	\$ -	\$ -	\$ 1,293,484
Residential	66,619,223	66,858,420	-	-	66,858,420
Policy loans	1,561,972	1,561,972	-	-	1,561,972
Short-term investments	50,004	50,004	50,004	-	-
Other long-term investments	41,658,491	52,418,704	-	-	52,418,704
Cash and cash equivalents	26,703,311	26,703,311	26,703,311	-	-
Accrued investment income	2,148,495	2,148,495	-	-	2,148,495
Loans from premium financing	68,223	68,223	-	-	68,223
Total financial assets	<u>\$ 140,087,799</u>	<u>\$ 151,102,613</u>	<u>\$ 26,753,315</u>	<u>\$ -</u>	<u>\$ 124,349,298</u>
Financial liabilities					
Policyholders' account balances	\$ 224,998,722	\$ 204,629,290	\$ -	\$ -	\$ 204,629,290
Policy claims	809,219	809,219	-	-	809,219
Total financial liabilities	<u>\$ 225,807,941</u>	<u>\$ 205,438,509</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 205,438,509</u>
December 31, 2015					
Financial assets					
Mortgage loans on real estate					
Commercial	\$ 1,464,655	\$ 1,486,601	\$ -	\$ -	\$ 1,486,601
Residential	57,310,263	57,356,546	-	-	57,356,546
Policy loans	1,486,317	1,486,317	-	-	1,486,317
Short-term investments	599,855	599,855	599,855	-	-
Other long-term investments	31,566,927	37,755,989	-	-	37,755,989
Cash and cash equivalents	9,047,586	9,047,586	9,047,586	-	-
Accrued investment income	2,205,469	2,205,469	-	-	2,205,469
Loans from premium financing	123,824	123,824	-	-	123,824
Total financial assets	<u>\$ 103,804,896</u>	<u>\$ 110,062,187</u>	<u>\$ 9,647,441</u>	<u>\$ -</u>	<u>\$ 100,414,746</u>
Financial liabilities					
Policyholders' account balances	\$ 197,688,616	\$ 179,233,152	\$ -	\$ -	\$ 179,233,152
Policy claims	714,928	714,928	-	-	714,928
Total financial liabilities	<u>\$ 198,403,544</u>	<u>\$ 179,948,080</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 179,948,080</u>

**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
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**3. Fair Value Measurements (continued)**

The estimated fair value amounts have been determined using available market information and appropriate valuation methodologies. However, considerable judgment was required to interpret market data to develop these estimates. Accordingly, the estimates are not necessarily indicative of the amounts which could be realized in a current market exchange. The use of different market assumptions or estimation methodologies may have a material effect on the fair value amounts.

The following methods and assumptions were used in estimating the fair value disclosures for financial instruments in the accompanying financial statements and notes thereto:

***Fixed Maturity Securities and Equity Securities***

The fair value of fixed maturity securities and equity securities are based on the principles previously discussed as Level 1, Level 2 and Level 3.

***Mortgage Loans on Real Estate***

The fair values for mortgage loans are estimated using discounted cash flow analyses. For residential mortgage loans, the discount rate used was indexed to the LIBOR yield curve adjusted for an appropriate credit spread. For commercial mortgage loans, the discount rate used was assumed to be the interest rate on the last commercial mortgage acquired by the Company.

***Cash and Cash Equivalents, Short-Term Investments, Accrued Investment Income, Policy Loans and Loans from Premium Financing***

The carrying value of these financial instruments approximates their fair values. Cash and cash equivalents and short-term investments are included in Level 1 of the fair value hierarchy due to their highly liquid nature.

***Other Long-Term Investments***

Other long-term investments are comprised of lottery prize receivables and fair value is derived by using a discounted cash flow approach. Projected cash flows are discounted using the average Citigroup Pension Liability Index in effect at the end of each period.

***Investment Contracts – Policyholders' Account Balances***

The fair value for liabilities under investment-type insurance contracts (accumulation annuities) is calculated using a discounted cash flow approach. Cash flows are projected using actuarial assumptions and discounted to the valuation date using risk-free rates adjusted for credit risk and the nonperformance risk of the liabilities.

The fair values for insurance contracts other than investment-type contracts are not required to be disclosed.

***Policy Claims***

The carrying amounts reported for these liabilities approximate their fair value.

**First Trinity Financial Corporation and Subsidiaries**  
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**(Unaudited)**

**4. Segment Data**

The Company has a life insurance segment, consisting of the life insurance operations of TLIC and FBLIC, an annuity segment, consisting of the annuity operations of TLIC and FBLIC and a corporate segment. Results for the parent company and the operations of FTCC, after elimination of intercompany amounts, are allocated to the corporate segment. These segments as of September 30, 2016 and December 31, 2015 and for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

	Three Months Ended September 30, (Unaudited)		Nine Months Ended September 30, (Unaudited)	
	2016	2015	2016	2015
Revenues:				
Life insurance operations	\$ 3,720,401	\$ 3,009,009	\$ 11,068,191	\$ 8,700,985
Annuity operations	2,802,934	2,688,858	8,158,645	7,094,580
Corporate operations	148,234	73,953	455,293	302,012
Total	<u>\$ 6,671,569</u>	<u>\$ 5,771,820</u>	<u>\$ 19,682,129</u>	<u>\$ 16,097,577</u>
Income (loss) before income taxes:				
Life insurance operations	\$ 35,230	\$ 752,366	\$ 87,745	\$ 754,556
Annuity operations	436,051	183,304	1,014,476	652,395
Corporate operations	115,591	(70,033)	235,444	134,988
Total	<u>\$ 586,872</u>	<u>\$ 865,637</u>	<u>\$ 1,337,665</u>	<u>\$ 1,541,939</u>
Depreciation and amortization expense:				
Life insurance operations	\$ 541,995	\$ 351,004	\$ 1,540,582	\$ 1,168,749
Annuity operations	154,648	224,704	493,151	570,215
Corporate operations	-	12,486	-	37,775
Total	<u>\$ 696,643</u>	<u>\$ 588,194</u>	<u>\$ 2,033,733</u>	<u>\$ 1,776,739</u>
	(Unaudited)			
	September 30, 2016	December 31, 2015		
Assets:				
Life insurance operations	\$ 50,073,485	\$ 44,151,860		
Annuity operations	256,044,991	218,172,909		
Corporate operations	6,946,066	6,805,073		
Total	<u>\$ 313,064,542</u>	<u>\$ 269,129,842</u>		

**5. Federal Income Taxes**

The provision for federal income taxes is based on the asset and liability method of accounting for income taxes. Deferred income taxes are provided for the cumulative temporary differences between balances of assets and liabilities determined under GAAP and the balances using tax bases. A valuation allowance has been established due to the uncertainty of certain loss carryforwards.

The Company has no known uncertain tax benefits within its provision for income taxes. In addition, the Company does not believe it would be subject to any penalties or interest relative to any open tax years and, therefore, has not accrued any such amounts. The Company files U.S. federal income tax returns and income tax returns in various state jurisdictions. The 2013 through 2015 U.S. federal tax years are subject to income tax examination by tax authorities. The Company classifies any interest and penalties (if applicable) as income tax expense in the financial statements.

**First Trinity Financial Corporation and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
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**6. Legal Matters and Contingent Liabilities**

The Company and Chairman, President and Chief Executive Officer, Gregg E. Zahn, filed an action in the District Court of Tulsa County, Oklahoma in 2013, Case No. CJ-2013-03385, against former Company Board of Directors member, Wayne Pettigrew and Mr. Pettigrew's company, Group & Pension Planners, Inc. (the "Defendants"). The petition filed in the case alleges that Mr. Pettigrew, during and after the time he was a member of the Company's Board of Directors, made defamatory statements regarding the Company and Mr. Zahn and committed breaches of his fiduciary duties to the Company. The defendants are alleged to have made defamatory statements to certain shareholders of the Company, to the press and to the Oklahoma Insurance Department and the Oklahoma Department of Securities. Mr. Pettigrew has denied the allegations.

The Board of Directors, represented by independent counsel, concluded that there was no action to be taken against Mr. Zahn and that the allegations by Mr. Pettigrew were without substance. The Company has been informed by the Oklahoma Insurance Department that it would take no action and also informed that the Oklahoma Department of Securities, after its investigation of the allegations, concluded that no proceedings were needed with respect to the alleged matters.

It is the Company's intention to vigorously prosecute this action against the Defendants for damages and for the correction of the defamatory statements. In the opinion of the Company's management, the ultimate resolution of any contingencies that may arise from this litigation is not considered material in relation to the financial position or results of operations of the Company.

Prior to its acquisition by TLIC, FBLIC developed, marketed, and sold life insurance products known as "Decreasing Term to 95" policies. On January 17, 2013, FBLIC's Board of Directors voted that, effective March 1, 2013, it was not approving, and therefore was not providing, a dividend for the Decreasing Term to 95 policies. On November 22, 2013, three individuals who owned Decreasing Term to 95 policies filed a Petition in the Circuit Court of Greene County, Missouri asserting claims against FBLIC relating to FBLIC's decision to not provide a dividend under the Decreasing Term to 95 policies.

On June 18, 2015, plaintiffs filed an amended petition. Like the original Petition, the amended Petition asserts claims for breach of contract and anticipatory breach of contract, and alleges that FBLIC breached, and will anticipatorily breach, the Decreasing Term to 95 policies of insurance by not providing a dividend sufficient to purchase a one year term life insurance policy which would keep the death benefit under the Decreasing Term to 95 policies the same as that provided during the first year of coverage under the policy. It also asserts claims for negligent misrepresentation, fraud, and violation of the Missouri Merchandising Practices Act ("MMPA"). It alleges that during its sale of the Decreasing Term to 95 policies, FBLIC represented that the owners of these policies would always be entitled to dividends to purchase a one-year term life insurance policy and that the owners would have a level death benefit without an increase in premium.

The main difference between the original Petition and the amended Petition is that the amended Petition also seeks equitable relief based on two new theories: that the Decreasing Term to 95 policies should be reformed so that they will provide a level death benefit for a level premium payment until the policyholder reaches 95 years of age; and alternatively, Count VIII of the amended Petition asks the Court to (1) find that the dividend provisions in the Decreasing Term to 95 policies violate Missouri law, specifically, § 376.360 RSMo.; (2) order that the policies are *void* ab initio; and (3) order that FBLIC return all premiums collected under these policies. In addition, as part of the MMPA claim, plaintiffs are now alleging that FBLIC undertook a fraudulent scheme to sell the Decreasing Term to 95 policies as a level premium for level benefit even though FBLIC never intended to pay dividends for the life of the policies and that part of this alleged fraudulent scheme included having a dividend option which is not allowed under Missouri law.

FBLIC denies the allegations in the amended Petition and will continue to defend against them.

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**6. Legal Matters and Contingent Liabilities (continued)**

On February 1, 2016, the plaintiffs asked that the Court certify the case as a class action. With their motion, Plaintiffs filed an affidavit from an actuary stating the opinion that FBLIC has collected at least \$2,548,939 in premiums on the Decreasing Term to 95 policies. This presumably is the amount that Plaintiffs will seek to be refunded to policyholders if the policies are declared void. FBLIC opposed the request for class certification. On July 21, 2016, the Court certified three classes to maintain the claims for breach of contract, anticipatory breach of contract, violation of the MMPA, reformation, and to void the Decreasing Term to 95 policies. On August 1, 2016, FBLIC filed a Petition for Leave to Appeal with the Missouri Court of Appeals, Southern District asking for permission to appeal the Court's class certification. The Petition for Leave to Appeal was denied.

FBLIC intends to defend vigorously against the class and individual allegations. The Company is unable to determine the potential magnitude of the claims in the event of a final certification and the plaintiffs prevailing on this substantive action.

On May 13, 2015, FBLIC filed a Counterclaim against Doyle Nimmo seeking indemnity and seeking damages for breach of fiduciary duty in the event FBLIC is liable under Plaintiffs' underlying claims. In addition, on April 29, 2015, TLIC filed a lawsuit against Doyle Nimmo and Michael Teel alleging that they were liable for violations of federal and state securities laws for failing to disclose information relating to the Decreasing Term to 95 policies. This lawsuit is currently pending in the District Court for the Western District of Missouri (hereinafter the "Federal Lawsuit"). No claims have been made against TLIC in the Federal Lawsuit. The Federal Lawsuit has been stayed pending resolution of the lawsuit against FBLIC in the Circuit Court of Greene County, Missouri.

On September 28, 2015, Doyle Nimmo filed a Third-Party Petition for Declaratory Judgment (and Other Relief) against FBLIC. In this Third-Party Petition, Doyle Nimmo, a former director for FBLIC, seeks a declaratory judgment that the corporate by-laws of FBLIC require FBLIC to indemnify him for attorney's fees, judgments, costs, fines, and amounts paid in defense of both the Counterclaim and the Federal Lawsuit and seeks a monetary judgment for the amounts expended by Doyle Nimmo in such defense. Prior to Doyle Nimmo's filing of the Third-Party Petition, FBLIC's Board of Directors executed a Unanimous Written Consent in Lieu of a Special Meeting in which it denied Doyle Nimmo's tender of defense and request for indemnification finding Mr. Nimmo did not meet the applicable standard of conduct for indemnification under Missouri law. FBLIC intends to vigorously defend the Third-Party Petition on these grounds. The Company is unable to determine the potential magnitude of the claims in the event Doyle Nimmo prevails on his Third-Party Petition.

As stated above, FBLIC filed a Counterclaim and TLIC filed the Federal Lawsuit against Doyle Nimmo. Doyle Nimmo submitted a claim and tendered the defense of these claims to Utica Mutual Insurance Company under a policy providing Insurance Agents and Brokers Errors and Omissions Liability coverage. On November 4, 2015, Utica Mutual Insurance Company filed a lawsuit against Doyle Nimmo and other interested parties, including FBLIC and TLIC. The lawsuit is pending in the District Court for the Western District of Missouri and asks the Court to determine whether the Errors and Omissions policy provides coverage for the lawsuits filed against Doyle Nimmo. Utica Mutual Insurance Company does not seek a monetary judgment against FBLIC or TLIC.

In most states, guaranty fund assessments may be taken as a credit against premium taxes, typically over a five-year period. These assessments, brought about by the insolvency of life and health insurers, are levied at the discretion of the various state guaranty fund associations to cover association obligations.

**First Trinity Financial Corporation and Subsidiaries**  
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**7. Other Comprehensive Income (Loss) and Accumulated Other Comprehensive Income (Loss)**

The changes in the components of the Company's accumulated other comprehensive income (loss) for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

	Unrealized Appreciation (Depreciation) on Available-For-Sale Securities	Adjustment to Deferred Acquisition Costs	Accumulated Other Comprehensive Income (Loss)
<u>Three Months Ended September 30, 2016 and 2015 (Unaudited)</u>			
Balance as of July 1, 2016	\$ 3,906,866	\$ (61,711)	\$ 3,845,155
Other comprehensive income before reclassifications, net of tax	846,814	(15,514)	831,300
Less amounts reclassified from accumulated other comprehensive income, net of tax	165,513	-	165,513
Other comprehensive income	681,301	(15,514)	665,787
Balance as of September 30, 2016	<u>\$ 4,588,167</u>	<u>\$ (77,225)</u>	<u>\$ 4,510,942</u>
Balance as of July 1, 2015	\$ 1,358,562	\$ (14,744)	\$ 1,343,818
Other comprehensive loss before reclassifications, net of tax	(1,219,333)	13,329	(1,206,004)
Less amounts reclassified from accumulated other comprehensive income (loss), net of tax	160,525	-	160,525
Other comprehensive loss	(1,379,858)	13,329	(1,366,529)
Balance as of September 30, 2015	<u>\$ (21,296)</u>	<u>\$ (1,415)</u>	<u>\$ (22,711)</u>
<u>Nine Months Ended September 30, 2016 and 2015 (Unaudited)</u>			
Balance as of January 1, 2016	\$ (2,695,876)	\$ 40,059	\$ (2,655,817)
Other comprehensive income before reclassifications, net of tax	7,552,715	(117,284)	7,435,431
Less amounts reclassified from accumulated other comprehensive income, net of tax	268,672	-	268,672
Other comprehensive income	7,284,043	(117,284)	7,166,759
Balance as of September 30, 2016	<u>\$ 4,588,167</u>	<u>\$ (77,225)</u>	<u>\$ 4,510,942</u>
Balance as of January 1, 2015	\$ 2,712,694	\$ (29,151)	\$ 2,683,543
Other comprehensive loss before reclassifications, net of tax	(2,748,807)	27,736	(2,721,071)
Less amounts reclassified from accumulated other comprehensive income (loss), net of tax	(14,817)	-	(14,817)
Other comprehensive loss	(2,733,990)	27,736	(2,706,254)
Balance as of September 30, 2015	<u>\$ (21,296)</u>	<u>\$ (1,415)</u>	<u>\$ (22,711)</u>



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**7. Other Comprehensive Income (Loss) and Accumulated Other Comprehensive Income (Loss) (continued)**

The pretax components of the Company's other comprehensive income (loss) and the related income tax expense (benefit) for each component for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

	Pretax	Income Tax Expense	Net of Tax
<u>Three Months Ended September 30, 2016 (Unaudited)</u>			
Other comprehensive income:			
Change in net unrealized gains on available-for-sale securities:			
Unrealized holding gains arising during the period	\$ 1,058,518	\$ 211,704	\$ 846,814
Reclassification adjustment for net gains included in operations	206,890	41,377	165,513
Net unrealized gains on investments	851,628	170,327	681,301
Adjustment to deferred acquisition costs	(19,392)	(3,878)	(15,514)
Total other comprehensive income	<u>\$ 832,236</u>	<u>\$ 166,449</u>	<u>\$ 665,787</u>
<u>Three Months Ended September 30, 2015 (Unaudited)</u>			
Other comprehensive loss:			
Change in net unrealized gains (losses) on available-for-sale securities:			
Unrealized holding losses arising during the period	\$ (1,524,166)	\$ (304,833)	\$ (1,219,333)
Reclassification adjustment for net gains included in operations	200,657	40,132	160,525
Net unrealized losses on investments	(1,724,823)	(344,965)	(1,379,858)
Adjustment to deferred acquisition costs	16,661	3,332	13,329
Total other comprehensive loss	<u>\$ (1,708,162)</u>	<u>\$ (341,633)</u>	<u>\$ (1,366,529)</u>
<u>Nine Months Ended September 30, 2016 (Unaudited)</u>			
Other comprehensive income:			
Change in net unrealized gains on available-for-sale securities:			
Unrealized holding gains arising during the period	\$ 9,440,894	\$ 1,888,179	\$ 7,552,715
Reclassification adjustment for net gains included in operations	335,841	67,169	268,672
Net unrealized gains on investments	9,105,053	1,821,010	7,284,043
Adjustment to deferred acquisition costs	(146,605)	(29,321)	(117,284)
Total other comprehensive income	<u>\$ 8,958,448</u>	<u>\$ 1,791,689</u>	<u>\$ 7,166,759</u>
<u>Nine Months Ended September 30, 2015 (Unaudited)</u>			
Other comprehensive loss:			
Change in net unrealized gains (losses) on available-for-sale securities:			
Unrealized holding losses arising during the period	\$ (3,436,009)	\$ (687,202)	\$ (2,748,807)
Reclassification adjustment for net losses included in operations	(18,521)	(3,704)	(14,817)
Net unrealized losses on investments	(3,417,488)	(683,498)	(2,733,990)
Adjustment to deferred acquisition costs	34,669	6,933	27,736
Total other comprehensive loss	<u>\$ (3,382,819)</u>	<u>\$ (676,565)</u>	<u>\$ (2,706,254)</u>

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**7. Other Comprehensive Income (Loss) and Accumulated Other Comprehensive Income (Loss) (continued)**

Realized gains and losses on the sales of investments are determined based upon the specific identification method and include provisions for other-than-temporary impairments where appropriate.

The pretax and the related income tax components of the amounts reclassified from the Company's accumulated other comprehensive income to the Company's consolidated statement of operations for the three and nine months ended September 30, 2016 and 2015 are summarized as follows:

Reclassification Adjustments	Three Months Ended September 30, (Unaudited)		Nine Months Ended September 30, (Unaudited)	
	2016	2015	2016	2015
Unrealized gains on available-for-sale securities:				
Realized gains (losses) on sales of securities (a)	\$ 206,890	\$ 200,657	\$ 335,841	\$ (18,521)
Income tax expense (benefit) (b)	41,377	40,132	67,169	(3,704)
Total reclassification adjustments	<u>\$ 165,513</u>	<u>\$ 160,525</u>	<u>\$ 268,672</u>	<u>\$ (14,817)</u>

(a) These items appear within net realized investment gains and loss on other-than-temporary impairment in the consolidated statements of operations.

(b) These items appear within federal income taxes in the consolidated statements of operations.

**8. Allowance for Loan Losses from Mortgage Loans on Real Estate and Loans from Premium Financing**

The allowance for possible loan losses from investments in mortgage loans on real estate and loans from premium financing is a reserve established through a provision for possible loan losses charged to expense which represents, in the Company's judgment, the known and inherent credit losses existing in the residential and commercial mortgage loan and premium financing loan portfolios. The allowance, in the judgment of the Company, is necessary to reserve for estimated loan losses inherent in the residential and commercial mortgage loan and premium finance loan portfolios and reduces the carrying value of investments in mortgage loans on real estate and premium finance loans to the estimated net realizable value on the consolidated statement of financial position.

While the Company utilizes its best judgment and information available, the ultimate adequacy of the allowance is dependent upon a variety of factors beyond the Company's control, including the performance of the residential and commercial mortgage loan and premium finance loan portfolios, the economy and changes in interest rates. The Company's allowance for possible mortgage loan and premium finance loan losses consists of specific valuation allowances established for probable losses on specific loans and a portfolio reserve for probable incurred but not specifically identified loans.

Mortgage loans and premium finance loans are considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the mortgage loan or premium finance loan agreement. Factors considered by the Company in determining impairment include payment status, collateral value of the real estate subject to the mortgage loan and the probability of collecting scheduled principal and interest payments when due. Mortgage loans and premium finance loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. The Company determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the mortgage loan or premium finance loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis.

As of September 30, 2016, \$525,696 of independent mortgage loan balances are held in escrow by a third party for the benefit of the Company related to its investment in \$23,962,879 of mortgage loans on real estate with one loan originator. In addition, the Company has an additional \$219,444 allowance for possible loan losses in the remaining

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\$43,934,424 of investments in mortgage loans on real estate as of September 30, 2016.

**8. Allowance for Loan Losses from Mortgage Loans on Real Estate and Loans from Premium Financing**  
(continued)

As of December 31, 2015, \$525,696 of independent mortgage loan balances are held in escrow by a third party for the benefit of the Company related to its investment in \$21,755,620 of mortgage loans on real estate with one loan originator. In addition, the Company has an additional \$183,348 allowance for possible loan losses in the remaining \$37,019,298 of investments in mortgage loans on real estate as of December 31, 2015.

Through June 30, 2012, FTCC financed amounts up to 80% of the premium on property and casualty insurance policies after a 20% or greater down payment was made by the policy owner. The premiums financed were collateralized by the amount of the unearned premium of the insurance policy. Policies that became delinquent were submitted for cancellation and recovery of the unearned premium, up to the amount of the loan balance, 25 days after a payment became delinquent. Loans from premium financing of \$347,885 and \$320,996 as of September 30, 2016 and December 31, 2015, respectively, are carried net of estimated loan losses of \$279,662 and \$197,172 as of September 30, 2016 and December 31, 2015, respectively. The Company has made no premium financing loans since June 30, 2012. FTCC currently has no operations other than minor premium refunds, collections of past due accounts and accounts involved in litigation.

The balances of and changes in the Company's credit losses related to mortgage loans on real estate and loans from premium financing as of and for the three and nine months ended September 30, 2016 and 2015 are summarized as follows (excluding \$23,962,879 and \$19,940,549 of mortgage loans on real estate as of September 30, 2016 and 2015, respectively, with one loan originator where independent mortgage loan balances are held in escrow by a third party for the benefit of the Company):

(Unaudited)

As of and for the Three Months Ended September 30,

	Residential Mortgage Loans		Commercial Mortgage Loans		Premium Finance Loans		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Allowance, beginning	\$ 191,332	\$ 156,254	\$ 6,532	\$ 8,204	\$ 279,662	\$ 197,171	\$ 477,526	\$ 361,629
Charge offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Provision	21,690	10,716	(110)	(123)	-	-	21,580	10,593
Allowance, ending	<u>\$ 213,022</u>	<u>\$ 166,970</u>	<u>\$ 6,422</u>	<u>\$ 8,081</u>	<u>\$ 279,662</u>	<u>\$ 197,171</u>	<u>\$ 499,106</u>	<u>\$ 372,222</u>
Allowance, ending:								
Individually evaluated for impairment	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 279,662</u>	<u>\$ 192,689</u>	<u>\$ 279,662</u>	<u>\$ 192,689</u>
Collectively evaluated for impairment	<u>\$ 213,022</u>	<u>\$ 166,970</u>	<u>\$ 6,422</u>	<u>\$ 8,081</u>	<u>\$ -</u>	<u>\$ 4,482</u>	<u>\$ 219,444</u>	<u>\$ 179,533</u>
Carrying Values:								
Individually evaluated for impairment	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 347,885</u>	<u>\$ 316,514</u>	<u>\$ 347,885</u>	<u>\$ 316,514</u>
Collectively evaluated for impairment	<u>\$ 42,656,344</u>	<u>\$ 33,536,288</u>	<u>\$ 1,278,080</u>	<u>\$ 1,608,114</u>	<u>\$ -</u>	<u>\$ 4,482</u>	<u>\$ 43,934,424</u>	<u>\$ 35,148,884</u>

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**8. Allowance for Loan Losses from Mortgage Loans on Real Estate and Loans from Premium Financing**  
(continued)

(Unaudited)

As of and for the Nine Months Ended September 30,

	Residential Mortgage Loans		Commercial Mortgage Loans		Premium Finance Loans		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Allowance, beginning	\$ 175,988	\$ 116,604	\$ 7,360	\$ 9,862	\$ 197,172	\$ 197,358	\$ 380,520	\$ 323,824
Charge offs	-	-	-	-	-	-	-	-
Recoveries	-	-	-	-	-	-	-	-
Provision	37,034	50,366	(938)	(1,781)	82,490	(187)	118,586	48,398
Allowance, ending	<u>\$ 213,022</u>	<u>\$ 166,970</u>	<u>\$ 6,422</u>	<u>\$ 8,081</u>	<u>\$ 279,662</u>	<u>\$ 197,171</u>	<u>\$ 499,106</u>	<u>\$ 372,222</u>
Allowance, ending:								
Individually evaluated for impairment	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 279,662</u>	<u>\$ 192,689</u>	<u>\$ 279,662</u>	<u>\$ 192,689</u>
Collectively evaluated for impairment	<u>\$ 213,022</u>	<u>\$ 166,970</u>	<u>\$ 6,422</u>	<u>\$ 8,081</u>	<u>\$ -</u>	<u>\$ 4,482</u>	<u>\$ 219,444</u>	<u>\$ 179,533</u>
Carrying Values:								
Individually evaluated for impairment	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 347,885</u>	<u>\$ 316,514</u>	<u>\$ 347,885</u>	<u>\$ 316,514</u>
Collectively evaluated for impairment	<u>\$ 42,656,344</u>	<u>\$ 33,536,288</u>	<u>\$ 1,278,080</u>	<u>\$ 1,608,114</u>	<u>\$ -</u>	<u>\$ 4,482</u>	<u>\$ 43,934,424</u>	<u>\$ 35,148,884</u>

The Company utilizes the ratio of the carrying value of individual residential and commercial mortgage loans compared to the individual appraisal value to evaluate the credit quality of its mortgage loans on real estate (commonly referred to as the loan-to-value ratio). The Company's residential and commercial mortgage loans on real estate by credit quality using this ratio as of September 30, 2016 and December 31, 2015 are summarized as follows:

	Residential Mortgage Loans		Commercial Mortgage Loans		Total Mortgage Loans	
	(Unaudited)		(Unaudited)		(Unaudited)	
Loan to Value Ratio	September 30, 2016	December 31, 2015	September 30, 2016	December 31, 2015	September 30, 2016	December 31, 2015
Over 70% to 80%	\$ 15,276,817	\$ 15,058,997	\$ -	\$ -	\$ 15,276,817	\$ 15,058,997
Over 60% to 70%	27,531,907	21,749,312	-	439,250	27,531,907	22,188,562
Over 50% to 60%	11,677,596	9,700,752	1,063,869	658,693	12,741,465	10,359,445
Over 40% to 50%	9,600,812	8,553,256	-	-	9,600,812	8,553,256
Over 30% to 40%	1,908,770	1,430,835	214,211	366,712	2,122,981	1,797,547
Over 20% to 30%	258,933	159,930	-	-	258,933	159,930
Over 10% to 20%	352,524	650,688	-	-	352,524	650,688
10% or less	11,864	6,493	-	-	11,864	6,493
Total	<u>\$ 66,619,223</u>	<u>\$ 57,310,263</u>	<u>\$ 1,278,080</u>	<u>\$ 1,464,655</u>	<u>\$ 67,897,303</u>	<u>\$ 58,774,918</u>

## **Item 2: Management’s Discussion and Analysis of Financial Condition and Results of Operations**

### **Overview**

First Trinity Financial Corporation (“we” “us”, “our”, “FTFC” or the “Company”) conducts operations as an insurance holding company emphasizing ordinary life insurance products in niche markets.

As an insurance provider, we collect premiums in the current period to pay future benefits to our policy and contract holders. Our core TLIC and FBLIC operations include issuing modified premium whole life insurance with a flexible premium deferred annuity, ordinary whole life, final expense, term and annuity products to predominately middle income households in the states of Alabama, Arizona, Arkansas, Colorado, Georgia, Illinois, Indiana, Kansas, Kentucky, Louisiana, Michigan, Mississippi, Missouri, Nebraska, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Pennsylvania, South Dakota, Tennessee, Texas, Utah, Virginia and West Virginia through independent agents.

We also realize revenues from our investment portfolio, which is a key component of our operations. The revenues we collect as premiums from policyholders are invested to ensure future benefit payments under the policy contracts. Life insurance companies earn profits on the investment spread, which reflects the investment income earned on the premiums paid to the insurer between the time of receipt and the time benefits are paid out under policies. Changes in interest rates, changes in economic conditions and volatility in the capital markets can all impact the amount of earnings that we realize from our investment portfolio.

### **Acquisitions**

The Company expects to facilitate growth through acquisitions of other life insurance companies and/or blocks of life insurance business.

In late December 2008, the Company completed its acquisition of 100% of the outstanding stock of FLAC, included in the life insurance and annuity segments, for \$2,500,000 and had additional acquisition related expenses of \$195,000. The acquisition of FLAC was financed with the working capital of FTFC.

In late December 2011, TLIC completed its acquisition of 100% of the outstanding stock of FBLIC, also included in the life insurance and annuity segments, for \$13,855,129. The acquisition of FBLIC was financed with the working capital of TLIC.

On April 28, 2015, the Company acquired a block of life insurance policies and annuity contracts according to the terms of an assumption reinsurance agreement. The Company acquired assets of \$3,644,839 (including cash), assumed liabilities of \$3,055,916 and recorded a gain on reinsurance assumption of \$588,923. During third quarter 2015, the Company completed its evaluation of assets, liabilities and gain associated with the reinsurance assumption and adjusted the assets, liabilities and gain on reinsurance assumption initially estimated and recorded in second quarter 2015.

Our profitability in the life insurance and annuity segments is a function of our ability to accurately price the policies that we write, adequately value life insurance business acquired, administer life insurance company acquisitions at an expense level that validates the acquisition cost and invest the premiums and annuity considerations in assets that earn investment income with a positive spread.

### **Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition, results of operations and liquidity and capital resources is based on our consolidated financial statements that have been prepared in accordance with U.S. GAAP. Preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. We evaluate our estimates and assumptions continually, including those related to investments, deferred acquisition costs, allowance for loan losses from mortgages and premium financing, value of insurance business acquired, policy liabilities, regulatory requirements, contingencies and litigation.

We base our estimates on historical experience and on various other factors and assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

For a description of the Company's critical accounting policies and estimates, please refer to "Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations - Critical Accounting Policies and Estimates" in the Company's Annual Report on Form 10-K for the year ended December 31, 2015. The Company considers its most critical accounting estimates to be those applied to investments in fixed maturity and equity securities, mortgage loans on real estate, deferred policy acquisition costs, value of insurance business acquired and future policy benefits. There have been no material changes to the Company's critical accounting policies and estimates since December 31, 2015.

### ***Recent Accounting Pronouncements***

#### *Revenue from Contracts with Customers*

In May 2014, the FASB issued updated guidance to clarify the principles for recognizing revenue. While insurance contracts are not within the scope of this updated guidance, the Company's fee income related to providing services will be subject to this updated guidance. The updated guidance requires an entity to recognize revenue as performance obligations are met, in order to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration the entity is entitled to receive for those goods or services.

The following steps are applied in the updated guidance: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract and (5) recognize revenue when, or as, the entity satisfies a performance obligation.

In July 2015, the FASB deferred the effective date of the updated guidance on revenue recognition by one year to the quarter ending March 31, 2018. The adoption of this guidance is not expected to have a material effect on the Company's result of operations, financial position or liquidity.

#### *Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period*

In June 2014, the FASB issued updated guidance to resolve diversity in practice concerning employee share-based payments that contain performance targets that could be achieved after the requisite service period. Many reporting entities account for performance targets that could be achieved after the requisite service period as performance conditions that affect the vesting of the award and, therefore, do not reflect the performance targets in the estimate of the grant-date fair value of the award. Other reporting entities treat those performance targets as nonvesting conditions that affect the grant-date fair value of the award.

The updated guidance requires that a performance target that affects vesting and that can be achieved after the requisite service period be treated as a performance condition. As such, the performance target that affects vesting should not be reflected in estimating that fair value of the award at the grant date. Compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the periods for which service has been rendered. If the performance target becomes probable of being achieved before the end of the service period, the remaining unrecognized compensation cost for which requisite service has not yet been rendered is recognized prospectively over the remaining service period. The total amount of compensation cost recognized during and after the service period should reflect the number of awards that are expected to vest and should be adjusted to reflect those awards that ultimately vest.

The updated guidance is effective for annual and interim periods beginning after December 15, 2015, with early adoption permitted. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

### *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*

In August 2014, the FASB issued guidance to address the diversity in practice in determining when there is substantial doubt about an entity's ability to continue as a going concern and when an entity must disclose certain relevant conditions and events. The new guidance requires an entity to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued). The new guidance allows the entity to consider the mitigating effects of management's plans that will alleviate the substantial doubt and requires certain disclosures when substantial doubt is alleviated as a result of consideration of management's plans.

If conditions or events raise substantial doubt that is not alleviated, an entity should disclose that there is substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued (or available to be issued), along with the principal conditions or events that raise substantial doubt, management's evaluation of the significance of those conditions or events in relation to the entity's ability to meet its obligations and management's plans that are intended to mitigate those conditions.

The guidance is effective for annual periods ending after December 15, 2016, and interim and annual periods thereafter. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

### *Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share Is More Akin to Debt or to Equity*

In November 2014, the FASB issued updated guidance to clarify when the separation of certain embedded derivative features in a hybrid financial instrument that is issued in the form of a share is required. That is, an entity will continue to evaluate whether the economic characteristics and risks of the embedded derivative feature are clearly and closely related to those of the host contract. Specifically, the amendments clarify that an entity should consider all relevant terms and features, including the embedded derivative feature being evaluated for bifurcation, in evaluating the nature of the host contract.

Furthermore, the amendments clarify that no single term or feature would necessarily determine the economic characteristics and risks of the host contract. Rather, the nature of the host contract depends upon the economic characteristics and risks of the entire hybrid financial instrument.

The updated guidance is effective for reporting periods beginning after December 15, 2015. Early adoption is permitted. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

### *Troubled Debt Restructurings by Creditors*

In January 2015, the FASB issued updated guidance for troubled debt restructurings clarifying when an in substance repossession or foreclosure occurs, and when a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan. The new guidance is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2015. This guidance can be elected for prospective adoption or by using a retrospective transition method. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

### *Amendments to the Consolidation Analysis*

In February 2015, the FASB issued updated guidance that makes targeted amendments to the current consolidation accounting guidance. The update is in response to accounting complexity concerns, particularly from the asset management industry. The guidance simplifies consolidation accounting by reducing the number of approaches to consolidation, provides a scope exception to registered money market funds and similar unregistered money market funds and ends the indefinite deferral granted to investment companies from applying the variable interest entity guidance.

The updated guidance is effective for annual and interim periods beginning after December 15, 2015. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

#### *Simplifying the Presentation of Debt Issuance Costs*

In April 2015, the FASB issued updated guidance to clarify the required presentation of debt issuance costs. The amended guidance requires that debt issuance costs be presented in the balance sheet as a direct reduction from the carrying amount of the recognized debt liability, consistent with the treatment of debt discounts. Amortization of debt issuance costs is to be reported as interest expense. The recognition and measurement guidance for debt issuance costs are not affected by the updated guidance. The updated guidance is effective for reporting periods beginning after December 15, 2015. Early adoption is permitted. The adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

#### *Simplifying the Accounting for Measurement-Period Adjustments*

In September 2015, the FASB issued updated guidance regarding business combinations that requires an acquirer to recognize post-close measurement adjustments for provisional amounts in the period the adjustment amounts are determined rather than retrospectively. The acquirer is also required to recognize, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the provisional amount, calculated as if the accounting had been completed at the acquisition date. The updated guidance is to be applied prospectively effective for annual and interim periods beginning after December 15, 2015. In connection with business combinations which have already been completed, the adoption of this guidance did not have a material effect on the Company's results of operations, financial position or liquidity.

#### *Recognition and Measurement of Financial Assets and Financial Liabilities*

In January 2016, the FASB issued updated guidance regarding financial instruments. This guidance intends to enhance reporting for financial instruments and addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The significant amendments in this update generally require equity investments to be measured at fair value with changes in fair value recognized in net income, require the use of an exit price notion when measuring the fair value of financial instruments for disclosure purposes and clarifies that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities. This guidance also intends to enhance the presentation of certain fair value changes for financial liabilities measured at fair value. It also amends certain disclosure requirements associated with the fair value of financial instruments.

This guidance is effective for fiscal years beginning after December 15, 2017. The recognition and measurement provisions of this guidance will be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption and early adoption is not permitted. The Company is evaluating this guidance but expects the primary impact will be the recognition of unrealized gains and losses on available-for-sale equity securities in net income. Currently, all unrealized gains and losses on available-for-sale equity securities are recognized in other comprehensive income (loss).

The effect of the adoption of this guidance on the Company's results of operations, financial position and liquidity is primarily dependent on the fair value of the available-for-sale equity securities in future periods and the existence of a deferred tax asset related to available-for-sale securities in future periods that have not yet been fully assessed.

#### *Leases*

In February 2016, the FASB issued updated guidance to require lessees to recognize a right-to-use asset and a lease liability for leases with terms of more than 12 months. The updated guidance retains the two classifications of a lease as either an operating or finance lease (previously referred to as a capital lease). Both lease classifications require the lessee to record the right-to-use asset and the lease liability based upon the present value of cash flows. Finance leases will reflect the financial arrangement by recognizing interest expense on the lease liability separately from the amortization expense of the right-to-use asset. Operating leases will recognize lease expense (with no separate recognition of interest expense) on a straight-line basis over the term of the lease. The accounting by lessors is not significantly changed by the updated guidance. The updated guidance requires expanded qualitative and quantitative disclosures, including additional information about the amounts recorded in the financial statements.



The updated guidance is effective for reporting periods beginning after December 15, 2018, and will require that the earliest comparative period presented include the measurement and recognition of existing leases with an adjustment to equity as if the updated guidance had always been applied. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

#### *Improvements to Employee Share-Based Payment Accounting*

In March 2016, the FASB issued updated guidance to simplify several aspects of accounting for share-based payment transactions as follows:

##### Accounting for Income Taxes

Under current accounting guidance, if the deduction for a share-based payment award for tax purposes exceeds, or is less than, the compensation cost recognized for financial reporting purposes, the resulting excess tax benefit, or tax deficiency, is reported as part of additional paid-in capital. Under the updated guidance, these excess tax benefits, or tax deficiencies, are reported as part of income tax expense or benefit in the income statement. The updated guidance also removes the requirement to delay recognition of any excess tax benefit when there are no current taxes payable to which the benefit would be applied. The tax-related cash flows resulting from share-based payments are to be included with other income tax cash flows as an operating activity rather than being reported separately as a financing activity.

##### Forfeitures

The updated guidance permits an entity to make an accounting policy election to either account for forfeitures when they occur or continue to apply the current method of accruing the compensation cost based on the number of awards that are expected to vest.

##### Minimum Statutory Tax Withholding Requirements

The updated guidance changes the threshold amount an entity can withhold for taxes when settling an equity award and still qualify for equity classification. A company can withhold up to the maximum statutory tax rates in the employees' applicable jurisdiction rather than withholding up to the employers' minimum statutory withholding requirement. The update also clarifies that all cash payments made to taxing authorities on behalf of employees for withheld shares are to be presented in financing activities on the statement of cash flows.

##### Transition

The updated guidance is effective for reporting periods beginning after December 15, 2016. Early adoption is permitted in any interim period; if early adoption is elected, the entity must adopt all of the amendments in the same reporting period and reflect any adjustments as of the beginning of the fiscal year. The Company has not elected early adoption. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

#### *Simplifying the Transition to the Equity Method of Accounting*

In March 2016, the FASB issued updated guidance that eliminates the requirement to retroactively apply the equity method of accounting when an investment that was previously accounted for using another method of accounting becomes qualified to apply the equity method due to an increase in the level of ownership interest or degree of influence. If the investment was previously accounted for as an available-for-sale security, any related unrealized gain or loss in accumulated other comprehensive income at the date the investment becomes qualified for the equity method is recognized through earnings. The updated guidance is effective for reporting periods beginning after December 15, 2016, and is to be applied prospectively. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

### *Contingent Put and Call Options in Debt Instruments*

In March 2016, the FASB issued updated guidance clarifying that when a call (put) option in a debt instrument can accelerate the repayment of principal on the debt instrument, a reporting entity does not need to assess whether the contingent event that triggers the ability to exercise the call (put) option is related to interest rates or credit risk in determining whether the option should be accounted for separately. The updated guidance is effective for reporting periods beginning after December 15, 2016. Early adoption is permitted. The adoption of this guidance is not expected to have a material effect on the Company's results of operations, financial position or liquidity.

### *Measurement of Credit Losses on Financial Instruments*

In June 2016, the FASB issued updated guidance for the accounting for credit losses for financial instruments. The updated guidance applies a new credit loss model (current expected credit losses or CECL) for determining credit-related impairments for financial instruments measured at amortized cost (e.g. reinsurance recoverables) and requires an entity to estimate the credit losses expected over the life of an exposure or pool of exposures. The estimate of expected credit losses should consider historical information, current information, as well as reasonable and supportable forecasts, including estimates of prepayments. The expected credit losses, and subsequent adjustments to such losses, will be recorded through an allowance account that is deducted from the amortized cost basis of the financial asset, with the net carrying value of the financial asset presented on the consolidated balance sheet at the amount expected to be collected.

The updated guidance also amends the current other-than-temporary impairment model for available-for-sale debt securities by requiring the recognition of impairments relating to credit losses through an allowance account and limits the amount of credit loss to the difference between a security's amortized cost basis and its fair value. In addition, the length of time a security has been in an unrealized loss position will no longer impact the determination of whether a credit loss exists. The updated guidance is effective for reporting periods beginning after December 15, 2019. Early adoption is permitted for reporting periods beginning after December 15, 2018. The Company will not be able to determine the impact that the updated guidance will have on its results of operations, financial position or liquidity until the updated guidance is adopted.

### *Classification of Certain Cash Receipts and Cash Payment*

In August 2016, the FASB issued new guidance that clarifies the classification of certain cash receipts and cash payments in the statement of cash flows under eight different scenarios including, but not limited to: (i) debt prepayment or debt extinguishment costs; (ii) proceeds from the settlement of corporate-owned life insurance policies including bank-owned life insurance policies; (iii) distributions received from equity method investees; and (iv) separately identifiable cash flows and application of the predominance principle. This guidance is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the impact of this guidance on our statement of cash flows.

### **Business Segments**

FASB guidance requires a "management approach" in the presentation of business segments based on how management internally evaluates the operating performance of business units. The discussion of segment operating results that follows is being provided based on segment data prepared in accordance with this methodology.

Our business segments are as follows:

- Life insurance operations, consisting of the life insurance operations of TLIC and FBLIC;
- Annuity operations, consisting of the annuity operations of TLIC and FBLIC and
- Corporate operations, which includes the results of the parent company and FTCC after the elimination of intercompany amounts.

Please see below and Note 4 to the Consolidated Financial Statements for the three and nine months ended September 30, 2016 and 2015 and as of September 30, 2016 and December 31, 2015 for additional information regarding segment information.

The following is a discussion and analysis of our financial condition, results of operations and liquidity and capital resources.

## FINANCIAL HIGHLIGHTS

### Consolidated Condensed Results of Operations for the Three Months Ended September 30, 2016 and 2015

	(Unaudited)		Amount Change 2016 less 2015	Percentage Change 2016 less 2015
	Three Months Ended September 30, 2016	2015		
Premiums	\$ 3,197,228	\$ 2,496,403	\$ 700,825	28.1%
Net investment income	3,303,980	2,916,317	387,663	13.3%
Net realized investment gains	160,308	280,763	(120,455)	-42.9%
Loss on other-than-temporary impairment	-	(1,078)	1,078	-100.0%
Gain on reinsurance assumption	-	38,923	(38,923)	-100.0%
Other income	10,053	40,492	(30,439)	-75.2%
Total revenues	6,671,569	5,771,820	899,749	15.6%
Benefits and claims	4,280,477	3,361,921	918,556	27.3%
Expenses	1,804,220	1,544,262	259,958	16.8%
Total benefits, claims and expenses	6,084,697	4,906,183	1,178,514	24.0%
Income before federal income tax expense	586,872	865,637	(278,765)	-32.2%
Federal income tax expense	88,286	217,920	(129,634)	-59.5%
Net income	<u>\$ 498,586</u>	<u>\$ 647,717</u>	<u>\$ (149,131)</u>	-23.0%
Net income per common share basic and diluted	<u>\$ 0.06</u>	<u>\$ 0.08</u>	<u>\$ (0.02)</u>	

### Consolidated Condensed Results of Operations for the Nine Months Ended September 30, 2016 and 2015

	(Unaudited)		Amount Change 2016 less 2015	Percentage Change 2016 less 2015
	Nine Months Ended September 30, 2016	2015		
Premiums	\$ 9,426,803	\$ 7,141,841	\$ 2,284,962	32.0%
Net investment income	9,922,817	7,828,639	2,094,178	26.8%
Net realized investment gains	307,250	786,852	(479,602)	-61.0%
Loss on other-than-temporary impairment	-	(305,334)	305,334	-100.0%
Gain on reinsurance assumption	-	588,923	(588,923)	-100.0%
Other income	25,259	56,656	(31,397)	-55.4%
Total revenues	19,682,129	16,097,577	3,584,552	22.3%
Benefits and claims	12,709,885	9,857,376	2,852,509	28.9%
Expenses	5,634,579	4,698,262	936,317	19.9%
Total benefits, claims and expenses	18,344,464	14,555,638	3,788,826	26.0%
Income before federal income tax expense	1,337,665	1,541,939	(204,274)	-13.2%
Federal income tax expense	205,667	160,586	45,081	28.1%
Net income	<u>\$ 1,131,998</u>	<u>\$ 1,381,353</u>	<u>\$ (249,355)</u>	-18.1%
Net income per common share basic and diluted	<u>\$ 0.15</u>	<u>\$ 0.18</u>	<u>\$ (0.03)</u>	

## Consolidated Condensed Financial Position as of September 30, 2016 and December 31, 2015

	(Unaudited) September 30, 2016	December 31, 2015	Amount Change 2016 less 2015	Percentage Change 2016 less 2015
Investment assets	\$ 248,989,318	\$ 230,203,402	\$ 18,785,916	8.2%
Other assets	64,075,224	38,926,440	25,148,784	64.6%
Total assets	<u>\$ 313,064,542</u>	<u>\$ 269,129,842</u>	<u>\$ 43,934,700</u>	16.3%
Policy liabilities	\$ 269,357,006	\$ 237,944,222	\$ 31,412,784	13.2%
Deferred federal income taxes	1,988,584	33,210	1,955,374	5887.9%
Other liabilities	3,205,152	937,367	2,267,785	241.9%
Total liabilities	274,550,742	238,914,799	35,635,943	14.9%
Shareholders' equity	38,513,800	30,215,043	8,298,757	27.5%
Total liabilities and shareholders' equity	<u>\$ 313,064,542</u>	<u>\$ 269,129,842</u>	<u>\$ 43,934,700</u>	16.3%
Shareholders' equity per common share	<u>\$ 4.94</u>	<u>\$ 3.87</u>	<u>\$ 1.07</u>	

## Results of Operations – Three Months Ended September 30, 2016 and 2015

### Revenues

Our primary sources of revenue are life insurance premium income and investment income. Premium payments are classified as first-year, renewal and single. In addition, realized gains and losses on investment holdings can significantly impact revenues from period to period.

Our revenues for the three months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited) Three Months Ended September 30, 2016	2015	Amount Change 2016 less 2015	Percentage Change 2016 less 2015
Premiums	\$ 3,197,228	\$ 2,496,403	\$ 700,825	28.1%
Net investment income	3,303,980	2,916,317	387,663	13.3%
Net realized investment gains	160,308	280,763	(120,455)	-42.9%
Loss on other-than-temporary impairment	-	(1,078)	1,078	-100.0%
Gain on reinsurance assumption	-	38,923	(38,923)	-100.0%
Other income	10,053	40,492	(30,439)	-75.2%
Total revenues	<u>\$ 6,671,569</u>	<u>\$ 5,771,820</u>	<u>\$ 899,749</u>	15.6%

The \$899,749 increase in total revenues for the three months ended September 30, 2016 is discussed below.

## Premiums

Our premiums for the three months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Three Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Whole life and term first year	\$ 44,599	\$ 26,756	\$ 17,843	66.7%
Whole life and term renewal	588,416	611,066	(22,650)	-3.7%
Final expense first year	920,613	633,523	287,090	45.3%
Final expense renewal	1,643,600	1,225,058	418,542	34.2%
Total premiums	\$ 3,197,228	\$ 2,496,403	\$ 700,825	28.1%

The \$700,825 increase in premiums for the three months ended September 30, 2016 is primarily due to a \$418,542 increase in final expense renewal premiums reflecting the persistency of prior years' final expense production. There was also a \$287,090 increase in final expense first year premiums due to increased production associated with contracting new, independent agents in expanded locations.

## Net Investment Income

The major components of our net investment income for the three months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Three Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Fixed maturity securities	\$ 1,435,041	\$ 1,400,291	\$ 34,750	2.5%
Equity securities	6,728	8,797	(2,069)	-23.5%
Other long-term investments	687,042	501,221	185,821	37.1%
Mortgage loans	1,417,445	1,172,040	245,405	20.9%
Policy loans	27,348	25,248	2,100	8.3%
Real estate	62,391	97,657	(35,266)	-36.1%
Short-term and other investments	56,806	46,018	10,788	23.4%
Gross investment income	3,692,801	3,251,272	441,529	13.6%
Investment expenses	(388,821)	(334,955)	53,866	-16.1%
Net investment income	\$ 3,303,980	\$ 2,916,317	\$ 387,663	13.3%

The \$441,529 increase in gross investment income for the three months ended September 30, 2016 is due to additional investments in mortgage loans, other long-term investments and fixed maturity securities. In the twelve months since September 30, 2015, our investments in mortgage loans have increased approximately \$12.8 million, other long term investments have increased approximately \$9.9 million and fixed maturity securities have increased approximately \$5.4 million.

The \$53,866 increase in investment expenses for the three months ended September 30, 2016 is primarily related to fees and expenses associated with mortgage loan investments due to the 2016 hiring of a mortgage loan director.

### ***Net Realized Investment Gains***

Our net realized investment gains result from sales of fixed maturity and equity securities available-for-sale and the early payoff gain (loss) of mortgage loans on real estate that the Company previously acquired.

Our net realized investment gains (losses) for the three months ended September 30, 2016 and 2015 and the \$120,455 decrease in net realized investment gains for the three months ended September 30, 2016 are summarized as follows:

	(Unaudited)			
	Three Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 to 2015
Fixed maturity securities available-for-sale:				
Proceeds from sales and maturities	\$ 7,368,724	\$ 4,983,682	\$ 2,385,042	47.9%
Amortized cost at sale date	7,161,834	4,781,947	2,379,887	49.8%
Net realized gains	<u>\$ 206,890</u>	<u>\$ 201,735</u>	<u>\$ 5,155</u>	2.6%
Mortgage loans on real estate:				
Payments and early payoffs of mortgage loans	\$ 7,655,905	\$ 3,328,222	\$ 4,327,683	130.0%
Principal collections	7,702,487	3,249,194	4,453,293	137.1%
Net realized gains (losses)	<u>\$ (46,582)</u>	<u>\$ 79,028</u>	<u>\$ (125,610)</u>	-158.9%
Net realized investment gains	<u>\$ 160,308</u>	<u>\$ 280,763</u>	<u>\$ (120,455)</u>	-42.9%

There were no impairments during the nine months ended September 30, 2016.

During second quarter and fourth quarter 2015, the Company impaired its bonds in a mining corporation with a total par value of \$600,000 as a result of an analysis of the mining corporation's ability to fulfill its obligations. This impairment was considered fully credit-related, resulting in a charge to the statement of operations before tax of \$304,256 and \$502,013 for the six months ended June 30, 2015 and year ended December 31, 2015, respectively. This charge represents the credit-related portion of the difference between the amortized cost basis of the security and its fair value. The Company experienced no additional other-than-temporary impairments during 2015.

On April 28, 2015, the Company acquired a block of life insurance policies and annuity contracts according to the terms of an assumption reinsurance agreement. The Company acquired assets of \$3,644,839 (including cash), assumed liabilities of \$3,055,916 and recorded a gain on reinsurance assumption of \$588,923. During third quarter 2015, the Company completed its evaluation of assets, liabilities and gain associated with the reinsurance assumption and adjusted the assets, liabilities and gain on reinsurance assumption initially estimated and recorded in second quarter 2015.

### **Total Benefits, Claims and Expenses**

Our benefits, claims and expenses are primarily generated from benefit payments, surrenders, interest credited to policyholders, change in reserves, commissions and other underwriting, insurance and acquisition expenses. Benefit payments can significantly impact expenses from period to period.

Our benefits, claims and expenses for the three months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Three Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
<b>Benefits and claims</b>				
Increase in future policy benefits	\$ 1,357,212	\$ 909,156	\$ 448,056	49.3%
Death benefits	881,928	803,941	77,987	9.7%
Surrenders	205,356	122,655	82,701	67.4%
Interest credited to policyholders	1,754,941	1,459,480	295,461	20.2%
Dividend, endowment and supplementary life contract benefits	81,040	66,689	14,351	21.5%
Total benefits and claims	4,280,477	3,361,921	918,556	27.3%
<b>Expenses</b>				
Policy acquisition costs deferred	(2,023,246)	(1,596,615)	(426,631)	26.7%
Amortization of deferred policy acquisition costs	536,901	428,448	108,453	25.3%
Amortization of value of insurance business acquired	91,966	92,561	(595)	-0.6%
Commissions	1,954,586	1,430,501	524,085	36.6%
Other underwriting, insurance and acquisition expenses	1,244,013	1,189,367	54,646	4.6%
Total expenses	1,804,220	1,544,262	259,958	16.8%
Total benefits, claims and expenses	\$ 6,084,697	\$ 4,906,183	\$ 1,178,514	24.0%

The \$1,178,514 increase in total benefits, claims and expenses for the three months ended September 30, 2016 is discussed below.

### ***Benefits and Claims***

The \$918,556 increase in benefits and claims for the three months ended September 30, 2016 is primarily due to the following:

- \$448,056 increase in future policy benefits is primarily related to the production of new policies, initial sales of policies to older age bands resulting in an increased mortality reserve charge and the aging of existing policies.
- \$295,461 increase in interest credited to policyholders is primarily due to an increase of approximately \$39.3 million in the amount of policyholders' account balances in the consolidated statement of financial position (increased deposits and interest credited in excess of withdrawals) since September 30, 2015.
- \$82,701 increase in surrenders is primarily due to a slight decrease in persistency of the life insurance in force.
- \$77,987 increase in death benefits is primarily due to final expense incurred claims. The increase in additional final expense incurred claims is expected by management due to the continued growth in the number of final expense policies in force.

### ***Deferral and Amortization of Deferred Acquisition Costs***

Certain costs related to the successful acquisition of traditional life insurance policies are capitalized and amortized over the premium-paying period of the policies. Certain costs related to the successful acquisition of insurance and annuity policies that subject us to mortality or morbidity risk over a period that extends beyond the period or periods in which premiums are collected and that have terms that are fixed and guaranteed (i.e., limited-payment long-duration annuity contracts) are capitalized and amortized in relation to the present value of actual and expected gross profits on the policies.

These acquisition costs, which are referred to as deferred policy acquisition costs, include commissions and other successful costs of acquiring life insurance, which vary with, and are primarily related to, the successful production of new and renewal insurance and annuity contracts.

For the three months ended September 30, 2016 and 2015, capitalized costs were \$2,023,246 and \$1,596,615, respectively. Amortization of deferred policy acquisition costs for the three months ended September 30, 2016 and 2015 were \$536,901 and \$428,448, respectively.

The \$426,631 increase in the acquisition costs deferred primarily relates to increased production of final expense products. The \$108,453 increase in the 2016 amortization of deferred acquisition costs is primarily due to a 2016 actuarial study that resulted in the reduction in the amount of 2016 acquisition expenses amortized by approximately \$100,000 during the third quarter 2016.

#### ***Amortization of Value of Insurance Business Acquired***

The cost of acquiring insurance business is amortized over the emerging profit of the related policies using the same assumptions that were used in computing liabilities for future policy benefits. Amortization of the value of insurance business acquired was \$91,966 and \$92,561 for the three months ended September 30, 2016 and 2015, respectively.

#### ***Commissions***

Our commissions for the three months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Three Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Annuity	\$ 652,377	\$ 526,498	\$ 125,879	23.9%
Whole life and term first year	30,368	28,909	1,459	5.0%
Whole life and term renewal	24,033	19,648	4,385	22.3%
Final expense first year	1,098,269	751,025	347,244	46.2%
Final expense renewal	149,539	104,421	45,118	43.2%
Total commissions	\$ 1,954,586	\$ 1,430,501	\$ 524,085	36.6%

The \$524,085 increase in commissions for the three months ended September 30, 2016 is primarily due to:

- \$347,244 increase in final expense first year commissions that correspond to the \$287,090 increase in final expense first year premiums.
- \$125,879 increase in annuity first year, single and renewal commissions is due to the Company now paying renewal commission on two annuity products amounting to \$134,338. These renewal commissions are half of the first year commissions and are paid if the annuity contract is still in force in the second year.

#### ***Other Underwriting, Insurance and Acquisition Expenses***

The \$54,646 increase in other underwriting, insurance and acquisition expenses for the three months ended September 30, 2016 was primarily related to increased acquisition and maintenance costs associated with increased final expense production and write-off of an uncollectible receivable from a prior year's sale of a portion of the premium finance business.



## ***Federal Income Taxes***

FTFC files a consolidated federal income tax return with FTCC but does not file a consolidated tax return with TLIC or FBLIC. TLIC and FBLIC are taxed as life insurance companies under the provisions of the Internal Revenue Code. Life insurance companies must file separate tax returns until they have been a member of the consolidated filing group for five years. However, we filed consolidated life insurance company federal tax returns for TLIC and FBLIC for 2013, 2014 and 2015 and intend to also file a consolidated life insurance company federal tax return for TLIC and FBLIC for 2016 during 2017.

Certain items included in income reported for financial statement purposes are not included in taxable income for the current period, resulting in deferred income taxes.

For the three months ended September 30, 2016 and 2015, current income tax expense was \$4,472 and \$218,754, respectively. Deferred federal income tax expense (benefit) was \$83,814 and (\$834) for the three months ended September 30, 2016 and 2015, respectively. The increase in deferred income taxes is primarily due to faster growth in deferred policy acquisition costs on the U.S. GAAP statement of financial position compared to the tax-basis balance sheet.

## ***Net Income Per Common Share Basic and Diluted***

Net income was \$498,586 (\$0.06 per common share basic and diluted) and \$647,717 (\$0.08 per common share basic and diluted) for the three months ended September 30, 2016 and 2015, respectively.

Net income per common share basic and diluted is calculated using the weighted average number of common shares outstanding and subscribed during the year. The weighted average outstanding and subscribed common shares basic and diluted were 7,802,593 for the three months ended September 30, 2016 and 2015.

## **Business Segments**

The Company has a life insurance segment, consisting of the life insurance operations of TLIC and FBLIC, an annuity segment, consisting of the annuity operations of TLIC and FBLIC and a corporate segment. Results for the parent company and the operations of FTCC, after elimination of intercompany amounts, are allocated to the corporate segment.

The revenues and income (loss) before federal income taxes from our business segments for the three months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Three Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Revenues:				
Life insurance operations	\$ 3,720,401	\$ 3,009,009	\$ 711,392	23.6%
Annuity operations	2,802,934	2,688,858	114,076	4.2%
Corporate operations	148,234	73,953	74,281	100.4%
Total	<u>\$ 6,671,569</u>	<u>\$ 5,771,820</u>	<u>\$ 899,749</u>	15.6%
Income (loss) before income taxes:				
Life insurance operations	\$ 35,230	\$ 752,366	\$ (717,136)	-95.3%
Annuity operations	436,051	183,304	252,747	137.9%
Corporate operations	115,591	(70,033)	185,624	265.1%
Total	<u>\$ 586,872</u>	<u>\$ 865,637</u>	<u>\$ (278,765)</u>	-32.2%

### ***Life Insurance Operations***

The \$711,392 increase in revenues from Life Insurance Operations for the three months ended September 30, 2016 is primarily due to the following:

- \$700,825 increase in premiums
- \$60,600 increase in net investment income
- \$30,439 decrease in other income
- \$19,594 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)

The \$717,136 decreased profitability from Life Insurance Operations for the three months ended September 30, 2016 is primarily due to the following:

- \$627,847 increase in other underwriting, insurance and acquisition expenses
- \$448,056 increase in future policy benefits
- \$398,206 increase in commissions
- \$82,701 increase in surrenders
- \$77,987 increase in death benefits
- \$30,439 decrease in other income
- \$19,594 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)
- \$14,351 increase in dividend, endowment and supplementary life contract benefits
- \$297 decrease in amortization of value of insurance business acquired
- \$60,600 increase in net investment income
- \$220,323 increase in policy acquisition costs deferred net of amortization
- \$700,825 increase in premiums

### ***Annuity Operations***

The \$114,076 increase in revenues from Annuity Operations for the three months ended September 30, 2016 is due to the following:

- \$252,782 increase in net investment income
- \$138,706 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)

The \$252,747 increased profitability from Annuity Operations for the three months ended September 30, 2016 is due to the following:

- \$461,858 decrease in other underwriting, insurance and acquisition expenses
- \$252,782 increase in net investment income
- \$97,855 increase in policy acquisition costs deferred net of amortization
- \$298 decrease in amortization of value of insurance business acquired
- \$125,879 increase in commissions
- \$138,706 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)
- \$295,461 increase in interest credited to policyholders

### ***Corporate Operations***

The \$74,281 increase in revenues from Corporate Operations for the three months ended September 30, 2016 is due to an increase in net investment income.

The \$185,624 increased Corporate Operations profitability for the three months ended September 30, 2016 is primarily due to \$111,343 of decreased operating expenses and \$74,281 of increased net investment income.

### **Results of Operations – Nine Months Ended September 30, 2016 and 2015**

#### **Revenues**

Our primary sources of revenue are life insurance premium income and investment income. Premium payments are classified as first-year, renewal and single. In addition, realized gains and losses on investment holdings can significantly impact revenues from period to period.

Our revenues for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Premiums	\$ 9,426,803	\$ 7,141,841	\$ 2,284,962	32.0%
Net investment income	9,922,817	7,828,639	2,094,178	26.8%
Net realized investment gains	307,250	786,852	(479,602)	-61.0%
Loss on other-than-temporary impairment	-	(305,334)	305,334	-100.0%
Gain on reinsurance assumption	-	588,923	(588,923)	-100.0%
Other income	25,259	56,656	(31,397)	-55.4%
Total revenues	<u>\$ 19,682,129</u>	<u>\$ 16,097,577</u>	<u>\$ 3,584,552</u>	22.3%

The \$3,584,552 increase in total revenues for the nine months ended September 30, 2016 is discussed below.

## Premiums

Our premiums for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Whole life and term first year	\$ 167,783	\$ 70,688	\$ 97,095	137.4%
Whole life and term renewal	1,857,418	1,917,350	(59,932)	-3.1%
Final expense first year	2,526,244	1,547,162	979,082	63.3%
Final expense renewal	4,496,784	3,540,645	956,139	27.0%
Supplementary contracts with life contingencies	378,574	65,996	312,578	473.6%
Total premiums	<u>\$ 9,426,803</u>	<u>\$ 7,141,841</u>	<u>\$ 2,284,962</u>	32.0%

The \$2,284,962 increase in premiums for the nine months ended September 30, 2016 is primarily due to the following: \$979,082 increase in final expense first year premiums, \$956,139 increase in final expense renewal premiums and \$312,578 increase in supplementary contracts with life contingencies premiums.

The increase in final expense first year premiums represents management's focus on expanding final expense production by contracting new, independent agents in expanded locations. The increase in final expense renewal premiums reflects the persistency of prior years' final expense production. Our marketing efforts are focused on final expense and annuity production and we have not been focused on whole life and term production the past few years.

The increase in supplementary contracts with life contingencies reflects policyholder decisions to receive future payment streams during their remaining life instead of a lump sum payment.

## Net Investment Income

The major components of our net investment income for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited) Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Fixed maturity securities	\$ 4,535,560	\$ 3,819,806	\$ 715,754	18.7%
Equity securities	20,568	29,051	(8,483)	-29.2%
Other long-term investments	1,857,366	1,340,050	517,316	38.6%
Mortgage loans	4,098,943	3,108,912	990,031	31.8%
Policy loans	79,937	75,554	4,383	5.8%
Real estate	246,327	357,067	(110,740)	-31.0%
Short-term and other investments	198,950	159,644	39,306	24.6%
Gross investment income	11,037,651	8,890,084	2,147,567	24.2%
Investment expenses	(1,114,834)	(1,061,445)	53,389	-5.0%
Net investment income	<u>\$ 9,922,817</u>	<u>\$ 7,828,639</u>	<u>\$ 2,094,178</u>	26.8%

The \$2,147,567 increase in gross investment income for the nine months ended September 30, 2016 is primarily due to the increases in investment in mortgage loans, fixed maturity securities and other long-term investments. In the twelve months since September 30, 2015, our investments in mortgage loans have increased approximately \$12.8 million, other long term investments have increased approximately \$9.9 million and fixed maturity securities have increased approximately \$5.4 million.

The \$110,740 decrease in real estate investment income is related to the loss of rental income from the sale of \$6,693,044 of real estate held for sale in March 2015.

The \$53,389 increase in investment expenses for the three months ended September 30, 2016 is primarily related to fees and expenses associated with mortgage loan investments due to the 2016 hiring of a mortgage loan director that was in excess of the 2015 investment expenses associated with the March 2015 sale of four real estate properties.

### ***Net Realized Investment Gains***

Our net realized investment gains result from sales of fixed maturity and equity securities available-for-sale and the early payoff gain (loss) of mortgage loans on real estate that the Company previously acquired.

Our net realized investment gains (losses) for the nine months ended September 30, 2016 and 2015 and the \$479,602 decrease in net realized investment gains for the nine months ended September 30, 2016 are summarized as follows:

	(Unaudited)		Amount Change 2016 less 2015	Percentage Change 2016 to 2015
	Nine Months Ended September 30, 2016	2015		
Fixed maturity securities available-for-sale:				
Sale proceeds	\$ 14,862,935	\$ 7,571,843	\$ 7,291,092	96.3%
Amortized cost at sale date	14,534,337	7,283,130	7,251,207	99.6%
Net realized gains	<u>\$ 328,598</u>	<u>\$ 288,713</u>	<u>\$ 39,885</u>	13.8%
Equity securities available-for-sale:				
Sale proceeds	\$ 128,010	\$ 533,813	\$ (405,803)	-76.0%
Cost at sale date	120,767	535,713	(414,946)	-77.5%
Net realized gains (losses)	<u>\$ 7,243</u>	<u>\$ (1,900)</u>	<u>\$ 9,143</u>	-481.2%
Mortgage loans on real estate:				
Payments and early payoffs of mortgage loans	\$ 11,317,427	\$ 7,452,257	\$ 3,865,170	51.9%
Principal collections	11,346,018	7,342,420	4,003,598	54.5%
Net realized gains (losses)	<u>\$ (28,591)</u>	<u>\$ 109,837</u>	<u>\$ (138,428)</u>	-126.0%
Investment real estate:				
Sale proceeds	\$ -	\$ 7,083,246	\$ (7,083,246)	-100.0%
Carrying value at sale date	-	6,693,044	(6,693,044)	-100.0%
Net realized gains	<u>\$ -</u>	<u>\$ 390,202</u>	<u>\$ (390,202)</u>	-100.0%
Net realized investment gains	<u>\$ 307,250</u>	<u>\$ 786,852</u>	<u>\$ (479,602)</u>	-61.0%

On March 11, 2015, the Company sold its investment real estate in buildings and land held for sale in Greensburg, Indiana; Norman, Oklahoma; Houston, Texas and Harrisonville, Missouri with an aggregate carrying value of \$6,693,044 as of March 11, 2015. The Company recorded a gross profit on these sales of \$390,202 based on an aggregate sales price of \$7,083,246 less closing costs and expenses of \$20,119.

During second quarter and fourth quarter 2015, the Company impaired its bonds in a mining corporation with a total par value of \$600,000 as a result of an analysis of the mining corporation's ability to fulfill its obligations. This impairment was considered fully credit-related, resulting in a charge to the statement of operations before tax of \$304,256 and \$502,013 for the six months ended June 30, 2015 and year ended December 31, 2015, respectively. This charge represents the credit-related portion of the difference between the amortized cost basis of the security and its fair value. The Company experienced no additional other-than-temporary impairments during 2015.

On April 28, 2015, the Company acquired a block of life insurance policies and annuity contracts according to the terms of an assumption reinsurance agreement. The Company acquired assets of \$3,644,839 (including cash), assumed liabilities of \$3,055,916 and recorded a gain on reinsurance assumption of \$588,923. During third quarter 2015, the Company completed its evaluation of assets, liabilities and gain associated with the reinsurance assumption and adjusted the assets, liabilities and gain on reinsurance assumption initially estimated and recorded in second quarter 2015.

### **Total Benefits, Claims and Expenses**

Our benefits, claims and expenses are primarily generated from benefit payments, surrenders, interest credited to policyholders, change in reserves, commissions and other underwriting, insurance and acquisition expenses. Benefit payments can significantly impact expenses from period to period.

Our benefits, claims and expenses for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Benefits and claims				
Increase in future policy benefits	\$ 3,995,230	\$ 2,605,117	\$ 1,390,113	53.4%
Death benefits	2,868,216	2,574,150	294,066	11.4%
Surrenders	541,725	400,536	141,189	35.3%
Interest credited to policyholders	5,090,162	4,052,780	1,037,382	25.6%
Dividend, endowment and supplementary life contract benefits	214,552	224,793	(10,241)	-4.6%
Total benefits and claims	12,709,885	9,857,376	2,852,509	28.9%
Expenses				
Policy acquisition costs deferred	(5,142,381)	(3,819,582)	(1,322,799)	34.6%
Amortization of deferred policy acquisition costs	1,588,938	1,285,997	302,941	23.6%
Amortization of value of insurance business acquired	281,175	291,918	(10,743)	-3.7%
Commissions	4,783,307	3,340,116	1,443,191	43.2%
Other underwriting, insurance and acquisition expenses	4,123,540	3,599,813	523,727	14.5%
Total expenses	5,634,579	4,698,262	936,317	19.9%
Total benefits, claims and expenses	\$ 18,344,464	\$ 14,555,638	\$ 3,788,826	26.0%

The \$3,788,826 increase in total benefits, claims and expenses for the nine months ended September 30, 2016 is discussed below.

### **Benefits and Claims**

The \$2,852,509 increase in benefits and claims for the nine months ended September 30, 2016 is primarily due to the following:

- \$1,390,113 increase in future policy benefits is primarily related to the production of new policies, initial sales of policies to older age bands resulting in an increased mortality reserve charge and the aging of existing policies.
- \$1,037,382 increase in interest credited to policyholders is primarily due to an increase of approximately \$39.3 million in the amount of policyholders' account balances in the consolidated statement of financial position (deposits and interest credited in excess of withdrawals) since September 30, 2015.

- \$294,066 increase in death benefits is primarily due to final expense claims incurred. The increase in additional final expense incurred claims is expected by the Company due to the continued growth in the number of final expense policies in force.
- \$141,189 increase in surrenders is primarily due to a slight decrease in persistency of the life insurance in force.

### ***Deferral and Amortization of Deferred Acquisition Costs***

Certain costs related to the successful acquisition of traditional life insurance policies are capitalized and amortized over the premium-paying period of the policies. Certain costs related to the successful acquisition of insurance and annuity policies that subject us to mortality or morbidity risk over a period that extends beyond the period or periods in which premiums are collected and that have terms that are fixed and guaranteed (i.e., limited-payment long-duration annuity contracts) are capitalized and amortized in relation to the present value of actual and expected gross profits on the policies. These acquisition costs, which are referred to as deferred policy acquisition costs, include commissions and other successful costs of acquiring life insurance, which vary with, and are primarily related to, the successful production of new and renewal insurance and annuity contracts.

For the nine months ended September 30, 2016 and 2015, capitalized costs were \$5,142,381 and \$3,819,582, respectively. Amortization of deferred policy acquisition costs for the nine months ended September 30, 2016 and 2015 were \$1,588,938 and \$1,285,997, respectively.

The \$1,322,799 increase in the 2016 acquisition costs deferred primarily relates to increased final expense production. The \$302,941 increase in the 2016 amortization of deferred acquisition costs is primarily due to the growth in the number of final expense policies in force combined with policies not being retained by policyholders. In addition, the increase in the 2016 amortization of deferred acquisition costs was impacted by the acceleration of amortization on annuity products from increased withdrawals. Finally, during 2016 we conducted an actuarial study that resulted in a reduction of the amount of 2016 acquisition expenses amortized by approximately \$100,000 during third quarter 2016.

### ***Amortization of Value of Insurance Business Acquired***

The cost of acquiring insurance business is amortized over the emerging profit of the related policies using the same assumptions that were used in computing liabilities for future policy benefits. Amortization of the value of insurance business acquired was \$281,175 and \$291,918 for the nine months ended September 30, 2016 and 2015, respectively.

### ***Commissions***

Our commissions for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Annuity	\$ 1,209,118	\$ 1,065,162	\$ 143,956	13.5%
Whole life and term first year	89,432	65,643	23,789	36.2%
Whole life and term renewal	77,099	79,048	(1,949)	-2.5%
Final expense first year	3,006,846	1,829,341	1,177,505	64.4%
Final expense renewal	400,812	300,922	99,890	33.2%
Total commissions	<u>\$ 4,783,307</u>	<u>\$ 3,340,116</u>	<u>\$ 1,443,191</u>	43.2%

The \$1,443,191 increase in commissions for the nine months ended September 30, 2016 is primarily due to:

- \$1,177,505 increase in final expense first year commissions that correspond to the \$979,082 increase in final expense first year premiums.

- \$143,956 increase in annuity first year, single and renewal commissions is due to the Company now paying renewal commission on two annuity products amounting to \$284,178. These renewal commissions are half of the first year commissions and are paid if the annuity contract is still in force in the second year.

#### ***Other Underwriting, Insurance and Acquisition Expenses***

The \$523,727 increase in other underwriting, insurance and acquisition expenses for the nine months ended September 30, 2016 was primarily related to increased acquisition and maintenance costs associated with increased final expense production, increased legal fees from contested litigation, increased salaries and benefits due to increased staffing levels, write-off and recording of bad debt expense of uncollectible receivables of the premium finance business and tenant improvements on the Topeka, Kansas office building.

#### ***Federal Income Taxes***

FTFC files a consolidated federal income tax return with FTCC but does not file a consolidated tax return with TLIC or FBLIC. TLIC and FBLIC are taxed as life insurance companies under the provisions of the Internal Revenue Code. Life insurance companies must file separate tax returns until they have been a member of the consolidated filing group for five years. However, we filed consolidated life insurance company federal tax returns for TLIC and FBLIC for 2013, 2014 and 2015 and intend to also file a consolidated life insurance company federal tax return for TLIC and FBLIC for 2016 during 2017.

Certain items included in income reported for financial statement purposes are not included in taxable income for the current period, resulting in deferred income taxes.

For the nine months ended September 30, 2016 and 2015, current income tax expense was \$41,982 and \$318,132, respectively. Deferred federal income tax expense (benefit) was \$163,685 and (\$157,546) for the nine months ended September 30, 2016 and 2015, respectively. The increase in deferred income taxes is primarily due to faster growth in deferred policy acquisition costs on the U.S. GAAP statement of financial position compared to the tax-basis balance sheet.

#### ***Net Income Per Common Share Basic and Diluted***

Net income was \$1,131,998 (\$0.15 per common share basic and diluted) and \$1,381,353 (\$0.18 per common share basic and diluted) for the nine months ended September 30, 2016 and 2015, respectively.

Net income per common share basic and diluted is calculated using the weighted average number of common shares outstanding and subscribed during the year. The weighted average outstanding and subscribed common shares basic and diluted for the nine months ended September 30, 2016 and 2015 were 7,802,593 and 7,805,223, respectively.

#### ***Business Segments***

The Company has a life insurance segment, consisting of the life insurance operations of TLIC and FBLIC, an annuity segment, consisting of the annuity operations of TLIC and FBLIC and a corporate segment. Results for the parent company and the operations of FTCC, after elimination of intercompany amounts, are allocated to the corporate segment.



The revenues and income before federal income taxes from our business segments for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)			
	Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 less 2015
Revenues:				
Life insurance operations	\$ 11,068,191	\$ 8,700,985	\$ 2,367,206	27.2%
Annuity operations	8,158,645	7,094,580	1,064,065	15.0%
Corporate operations	455,293	302,012	153,281	50.8%
Total	<u>\$ 19,682,129</u>	<u>\$ 16,097,577</u>	<u>\$ 3,584,552</u>	22.3%
Income before income taxes:				
Life insurance operations	\$ 87,745	\$ 754,556	\$ (666,811)	-88.4%
Annuity operations	1,014,476	652,395	362,081	55.5%
Corporate operations	235,444	134,988	100,456	74.4%
Total	<u>\$ 1,337,665</u>	<u>\$ 1,541,939</u>	<u>\$ (204,274)</u>	-13.2%

### ***Life Insurance Operations***

The \$2,367,206 increase in revenues from Life Insurance Operations for the nine months ended September 30, 2016 is primarily due to the following:

- \$2,284,962 increase in premiums
- \$250,810 increase in net investment income
- \$34,626 decrease in other income
- \$133,940 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)

The \$666,811 decreased profitability from Life Insurance Operations for the nine months ended September 30, 2016 is primarily due to the following:

- \$1,390,113 increase in future policy benefits
- \$1,299,235 increase in commissions
- \$903,614 increase in other underwriting, insurance and acquisition expenses
- \$294,066 increase in death benefits
- \$141,189 increase in surrenders
- \$133,940 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)
- \$34,626 decrease in other income
- \$5,371 decrease in amortization of value of insurance business acquired
- \$10,241 decrease in dividend, endowment and supplementary life contract benefits
- \$250,810 increase in net investment income

- \$978,588 increase in policy acquisition costs deferred net of amortization
- \$2,284,962 increase in premiums

### ***Annuity Operations***

The \$1,064,065 increase in revenues from Annuity Operations for the nine months ended September 30, 2016 is due to the following:

- \$1,693,316 increase in net investment income
- \$629,251 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)

The \$362,081 increased profitability from Annuity Operations for the nine months ended September 30, 2016 is due to the following:

- \$1,693,316 increase in net investment income
- \$432,712 decrease in other underwriting, insurance and acquisition expenses
- \$41,270 increase in policy acquisition costs deferred net of amortization
- \$5,372 decrease in amortization of value of insurance business acquired
- \$143,956 increase in commissions
- \$629,251 decrease in net realized investment gains (that also includes a loss on other-than-temporary impairment and gain on reinsurance assumption)
- \$1,037,382 increase in interest credited to policyholders

### ***Corporate Operations***

The \$153,281 increase in revenues from Corporate Operations for the nine months ended September 30, 2016 is primarily due to \$150,052 of increased net investment income and \$3,229 of increased other income.

The \$100,456 increased Corporate Operations profitability for the nine months ended September 30, 2016 is primarily due to \$150,052 of increased net investment income and \$3,229 of increased other income that exceeded \$52,825 of increased operating expenses.

## Consolidated Financial Condition

Our invested assets as of September 30, 2016 and December 31, 2015 are summarized as follows:

	(Unaudited) September 30, 2016	December 31, 2015	Amount Change 2016 less 2015	Percentage Change 2016 less 2015
<b>Assets</b>				
Investments				
Available-for-sale fixed maturity securities at fair value (amortized cost: \$128,986,347 and \$138,028,455 as of September 30, 2016 and December 31, 2015, respectively)	\$ 134,592,061	\$ 134,556,027	\$ 36,034	0.0%
Available-for-sale equity securities at fair value (cost: \$683,928 and \$790,215 as of September 30, 2016 and December 31, 2015, respectively)	813,424	892,800	(79,376)	-8.9%
Mortgage loans on real estate	67,897,303	58,774,918	9,122,385	15.5%
Investment real estate	2,416,063	2,326,558	89,505	3.8%
Policy loans	1,561,972	1,486,317	75,655	5.1%
Short-term investments	50,004	599,855	(549,851)	-91.7%
Other long-term investments	41,658,491	31,566,927	10,091,564	32.0%
Total investments	<u>\$ 248,989,318</u>	<u>\$ 230,203,402</u>	<u>\$ 18,785,916</u>	<u>8.2%</u>

The \$36,034 and \$18,507,331 increases in fixed maturity available-for-sale securities for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	Nine Months Ended September 30, (Unaudited)			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Fixed maturity securities, available-for-sale, beginning	\$ 134,556,027	99.97%	\$ 110,651,429	85.67%
Purchases	6,163,564	4.59%	26,575,622	20.58%
Assumption reinsurance	-	0.00%	3,534,093	2.74%
Unrealized appreciation (depreciation)	9,078,142	6.74%	(3,345,103)	-2.59%
Net realized investment gains (losses)	328,598	0.24%	(16,621)	-0.01%
Sales proceeds	(10,205,935)	-7.58%	(5,937,843)	-4.60%
Maturities	(4,657,000)	-3.46%	(1,634,000)	-1.27%
Premium amortization	(671,335)	-0.50%	(668,817)	-0.52%
Increase	<u>36,034</u>	<u>0.03%</u>	<u>18,507,331</u>	<u>14.33%</u>
Fixed maturity securities, available-for-sale, ending	<u>\$ 134,592,061</u>	<u>100.00%</u>	<u>\$ 129,158,760</u>	<u>100.00%</u>

Fixed maturity securities available-for-sale are reported at fair value with unrealized gains and losses, net of applicable income taxes, reflected as a separate component in shareholders' equity within "Accumulated Other Comprehensive Income (Loss)." The available-for-sale fixed maturity securities portfolio is invested primarily in a variety of companies, U. S. government and government agencies, states and political subdivisions and foreign securities.

The \$79,376 and \$57,068 decreases in equity securities available-for-sale for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	Nine Months Ended September 30, (Unaudited)			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Equity securities, available-for-sale, beginning	\$ 892,800	109.76%	\$ 671,357	109.29%
Purchases	14,480	1.78%	551,229	89.73%
Sales proceeds	(128,010)	-15.74%	(533,813)	-86.90%
Unrealized appreciation (depreciation)	26,911	3.31%	(72,385)	-11.78%
Net realized investment gains (losses)	7,243	0.89%	(1,900)	-0.31%
Premium amortization	-	0.00%	(199)	-0.03%
Decrease	(79,376)	-9.76%	(57,068)	-9.29%
Equity securities, available-for-sale, ending	<u>\$ 813,424</u>	<u>100.00%</u>	<u>\$ 614,289</u>	<u>100.00%</u>

Equity securities available-for-sale are also reported at fair value with unrealized gains and losses, net of applicable income taxes, reflected as a separate component in shareholders' equity within "Accumulated Other Comprehensive Income (Loss)." The available-for-sale equity securities portfolio is invested in a small number of companies.

The \$9,122,385 and \$16,435,218 increases in mortgage loans on real estate for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	Nine Months Ended September 30, (Unaudited)			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Mortgage loans on real estate, beginning	\$ 58,774,918	86.56%	\$ 38,649,733	70.16%
Purchases	20,669,087	30.44%	23,665,861	42.97%
Capitalization of loan origination fees	4,530	0.01%	74,000	0.13%
Discount accretion	83,536	0.12%	137,724	0.25%
Net realized investment gains (losses)	(28,591)	-0.04%	109,837	0.20%
Payments	(11,317,427)	-16.67%	(7,452,257)	-13.53%
Foreclosed - transferred to real estate	(198,622)	-0.29%	-	0.00%
Increase in allowance for bad debts	(36,096)	-0.05%	(48,585)	-0.09%
Amortization of loan origination fees	(54,032)	-0.08%	(51,362)	-0.09%
Increase	9,122,385	13.44%	16,435,218	29.84%
Mortgage loans on real estate, ending	<u>\$ 67,897,303</u>	<u>100.00%</u>	<u>\$ 55,084,951</u>	<u>100.00%</u>

The \$89,505 increase and \$6,802,161 decrease in investment real estate for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	Nine Months Ended September 30, (Unaudited)			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Investment real estate, beginning	\$2,326,558	96.30%	\$ 9,165,090	387.87%
Real estate acquired through mortgage loan foreclosure	198,622	8.22%	-	0.00%
Sales proceeds	-	0.00%	(7,083,246)	-299.76%
Depreciation of building	(109,117)	-4.52%	(109,117)	-4.62%
Net realized investment gains	-	0.00%	390,202	16.51%
Increase (decrease)	89,505	3.70%	(6,802,161)	-287.87%
Investment real estate, ending	\$2,416,063	100.00%	\$ 2,362,929	100.00%

The \$10,091,564 and \$10,012,751 increases in other long-term investments (composed of lottery receivables) for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	Nine Months Ended September 30, (Unaudited)			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Other long-term investments, beginning	\$ 31,566,927	75.78%	\$21,781,925	68.51%
Purchases	11,340,463	27.22%	11,968,198	37.64%
Accretion of discount	1,865,829	4.48%	1,289,624	4.06%
Payments	(3,114,728)	-7.48%	(3,245,071)	-10.21%
Increase	10,091,564	24.22%	10,012,751	31.49%
Other long-term investments, ending	\$ 41,658,491	100.00%	\$31,794,676	100.00%

The \$549,851 decrease in short-term investments is due to management's decision to decrease our investment in funds that have a maturity of more than 90 days but less than one year at the date of purchase.

Our assets other than invested assets as of September 30, 2016 and December 31, 2015 are summarized as follows:

	(Unaudited)		Amount Change 2016 less 2015	Percentage Change 2016 less 2015
	September 30, 2016	December 31, 2015		
Cash and cash equivalents	\$ 26,703,311	\$ 9,047,586	\$ 17,655,725	195.1%
Accrued investment income	2,148,495	2,205,469	(56,974)	-2.6%
Recoverable from reinsurers	1,281,156	1,243,618	37,538	3.0%
Agents' balances and due premiums	1,414,608	1,070,050	344,558	32.2%
Deferred policy acquisition costs	16,422,517	13,015,679	3,406,838	26.2%
Value of insurance business acquired	6,007,025	6,288,200	(281,175)	-4.5%
Other assets	10,098,112	6,055,838	4,042,274	66.8%
Assets other than investment assets	\$ 64,075,224	\$ 38,926,440	\$ 25,148,784	64.6%

The \$344,558 increase in 2016 agents' balances and due premiums is primarily due to a \$352,229 increase in agents' balances. This increase is due to increased production of final expense policies resulting in increased advances of commissions to agents. The Company closely monitors commission advances and has not historically experienced nor expects to experience future collection problems.

Our other assets as of September 30, 2016 and December 31, 2015 are summarized as follows:

	(Unaudited)		Amount Change	Percentage Change
	September 30, 2016	December 31, 2015	2016 less 2015	2016 to 2015
Advances to mortgage loan originator	\$ 5,561,084	\$ 3,095,064	\$ 2,466,020	79.7%
Federal and state income taxes recoverable	1,742,437	1,265,453	476,984	37.7%
Notes receivable	493,804	627,503	(133,699)	-21.3%
Accrual of mortgage loan and long-term investment payments due	1,975,403	662,354	1,313,049	198.2%
Guaranty funds	189,911	197,812	(7,901)	-4.0%
Loans from premium financing, net	68,223	123,824	(55,601)	-44.9%
Other receivables, prepaid assets and deposits	67,250	83,828	(16,578)	-19.8%
Total other assets	<u>\$ 10,098,112</u>	<u>\$ 6,055,838</u>	<u>\$ 4,042,274</u>	66.8%

During the nine months ended September 30, 2016, the Company increased its advances to one mortgage loan originator who acquires residential mortgage loans for our life insurance companies by \$2,466,020.

There was a \$1,313,049 increase in the accrual of mortgage loans and long-term investment payments based upon the scheduled timing of investment payments remitted by the third party servicers.

The \$476,984 increase in federal and state income taxes recoverable is primarily due to federal and state tax withholdings on lottery receivables.

On April 15, 2016, the Company renewed its previous one-year loan of \$400,000 to its former Chairman. The renewed loan also has a term of one year and a contractual interest rate of 5.00%. The loan is collateralized by 100,000 shares of the Company's Class A Common stock owned by the former Chairman.

Our liabilities as of September 30, 2016 and December 31, 2015 are summarized as follows:

	(Unaudited)		Amount Change	Percentage Change
	September 30, 2016	December 31, 2015	2016 less 2015	2016 less 2015
Policy liabilities				
Policyholders' account balances	\$ 224,998,722	\$ 197,688,616	\$ 27,310,106	13.8%
Future policy benefits	43,466,880	39,464,124	4,002,756	10.1%
Policy claims	809,219	714,928	94,291	13.2%
Other policy liabilities	82,185	76,554	5,631	7.4%
Total policy liabilities	<u>269,357,006</u>	<u>237,944,222</u>	<u>31,412,784</u>	13.2%
Deferred federal income taxes	1,988,584	33,210	1,955,374	5887.9%
Other liabilities	<u>3,205,152</u>	<u>937,367</u>	<u>2,267,785</u>	241.9%
Total liabilities	<u>\$ 274,550,742</u>	<u>\$ 238,914,799</u>	<u>\$ 35,635,943</u>	14.9%

The \$27,310,106 and \$45,193,198 increases in policyholders' account balances for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	Nine Months Ended September 30, (Unaudited)			
	2016		2015	
	Amount	Percentage	Amount	Percentage
Policyholders' account balances, beginning	\$ 197,688,616	87.86%	\$ 140,554,973	75.67%
Deposits	32,177,094	14.31%	45,590,381	24.55%
Assumption reinsurance	-	0.00%	2,966,827	1.59%
Withdrawals	(9,957,150)	-4.43%	(7,416,790)	-3.99%
Interest credited	5,090,162	2.26%	4,052,780	2.18%
Increase	27,310,106	12.14%	45,193,198	24.33%
Policyholders' account balances, ending	<u>\$ 224,998,722</u>	<u>100.00%</u>	<u>\$ 185,748,171</u>	<u>100.00%</u>

During 2016, management made a conscious decision to decrease the production of new annuity contracts by decreasing the interest rate paid to policyholders and the minimum guaranteed interest rate during the contractual period. This intentional reduction in new annuity production is demonstrated by the \$13,413,287 decrease in annuity deposits from \$45,590,381 to \$32,177,094 for the nine months ended September 30, 2015 and 2016, respectively. This decision was made so that FTFC's two life insurance companies, TLIC and FBLIC, can improve their statutory solvency by increasing the ratio of the total statutory adjusted capital to the statutory authorized control level risk-based capital in both TLIC and FBLIC.

The \$4,002,756 increase in future policy benefits during the nine months ended September 30, 2016 is primarily related to the production of new life insurance policies, initial sales of policies to older age bands (resulting in increased mortality reserve charges) and the aging of existing policies.

The \$1,955,374 increase in deferred federal income taxes during the nine months ended September 30, 2016 was due to \$1,791,689 of increased deferred federal income taxes on the unrealized appreciation of fixed maturity and equity securities available-for-sale and \$163,685 of operating deferred federal tax expense.

Our other liabilities as of September 30, 2016 and December 31, 2015 are summarized as follows:

	(Unaudited)		Amount Change	Percentage Change
	September 30, 2016	December 31, 2015	2016 less 2015	2016 to 2015
Suspense accounts payable	\$ 2,395,266	\$ 175,134	\$ 2,220,132	1267.7%
Accrued expenses payable	479,036	405,726	73,310	18.1%
Guaranty fund assessments	172,000	172,000	-	0.0%
Unclaimed funds	38,251	45,504	(7,253)	-15.9%
Unearned investment income	50,745	53,945	(3,200)	-5.9%
Deferred revenue	31,608	34,949	(3,341)	-9.6%
Withholdings payable	8,626	31,015	(22,389)	-72.2%
Other payables	29,620	19,094	10,526	55.1%
Total other liabilities	<u>\$ 3,205,152</u>	<u>\$ 937,367</u>	<u>\$ 2,267,785</u>	241.9%

The \$2,220,132 increase in suspense accounts payable is primarily due to increased deposits on policy applications that had not been issued as of the financial reporting date.

## Liquidity and Capital Resources

Our operations have been financed primarily through the private placement of equity securities and intrastate public stock offerings. Through September 30, 2016, we have received \$27,119,480 from the sale of our shares.

The Company raised \$1,450,000 from two private placements during 2004 and \$25,669,480 from two public stock offerings and one private placement stock offering from June 22, 2005 through February 23, 2007; June 29, 2010 through April 30, 2012; and August 15, 2012 through March 8, 2013. The Company issued 7,347,488 shares of its common stock and incurred \$3,624,518 of offering costs during these private placements and public stock offerings.

The Company also issued 702,685 shares of its common stock in connection with two stock dividends paid to shareholders in 2011 and 2012 that resulted in accumulated earnings being charged \$5,270,138 with an offsetting credit of \$5,270,138 to common stock and additional paid-in capital.

The Company has also purchased 247,580 shares of treasury stock at a cost of \$893,947 from former members of the Board of Directors including the former Chairman of the Board of Directors, a former agent, the former spouse of the Company's Chairman, Chief Executive Officer and President and a charitable organization where a former member of the Board of Directors had donated shares of the Company's common stock.

As of September 30, 2016, we had cash and cash equivalents totaling \$26,703,311. As of September 30, 2016, cash and cash equivalents of \$11,871,837 and \$13,227,837, respectively, were held by FBLIC and TLIC and may not be available for use by FTFC due to the required pre-approval by the OID and Missouri Department of Insurance of any dividend or intercompany transaction to transfer funds to FTFC. The maximum dividend, which may be paid in any twelve-month period without notification or approval, is limited to the greater of 10% of statutory surplus as of December 31 of the preceding year or the net gain from operations of the preceding calendar year.

Cash dividends may only be paid out of surplus derived from realized net profits. Based on these limitations, there is capacity for TLIC to pay a dividend up to \$2,266,305 in 2016 without prior approval. In addition, based on those limitations, there is the capacity for FBLIC to pay a dividend up to \$915,147 in 2016 without prior approval. FBLIC paid dividends of \$1,000,000 in 2015. Through September 30, 2016, FBLIC has paid no dividends in 2016. The 2015 dividend is eliminated in consolidation. TLIC has paid no dividends to FTFC.

The Company maintains cash and cash equivalents at multiple institutions. The Federal Deposit Insurance Corporation insures interest and non-interest bearing accounts up to \$250,000. Uninsured balances aggregate \$15,210,065 and \$5,957,248 as of September 30, 2016 and December 31, 2015, respectively. The increase in uninsured balances of \$9,252,817 between September 30, 2016 and December 31, 2015 is primarily due to annuity production in the third quarter 2016 that has yet to be invested. Other funds are invested in mutual funds that invest in U.S. government securities. We monitor the solvency of all financial institutions in which we have funds to minimize the exposure for loss. The Company has not experienced any losses in such accounts.

Our cash flows for the nine months ended September 30, 2016 and 2015 are summarized as follows:

	(Unaudited)		Amount Change 2016 less 2015	Percentage Change 2016 less 2015
	Nine Months Ended September 30, 2016	2015		
Net cash provided by operating activities	\$ 4,200,275	\$ 4,571,653	\$ (371,378)	-8.1%
Net cash used in investing activities	(8,764,494)	(36,809,745)	28,045,251	-76.2%
Net cash provided by financing activities	22,219,944	34,058,475	(11,838,531)	-34.8%
Increase in cash	17,655,725	1,820,383	15,835,342	869.9%
Cash and cash equivalents, beginning of period	9,047,586	10,158,386	(1,110,800)	-10.9%
Cash and cash equivalents, end of period	<u>\$ 26,703,311</u>	<u>\$ 11,978,769</u>	<u>\$ 14,724,542</u>	122.9%



The \$4,200,275 and \$4,571,653 of cash provided by operating activities for the nine months ended September 30, 2016 and 2015, respectively, are summarized as follows:

	(Unaudited)			
	Nine Months Ended September 30,		Amount Change	Percentage Change
	2016	2015	2016 less 2015	2016 to 2015
Premiums collected	\$ 9,441,443	\$ 7,149,408	2,292,035	32.1%
Net investment income collected	7,385,512	6,211,324	1,174,188	18.9%
Death benefits paid	(2,811,463)	(2,496,394)	(315,069)	12.6%
Surrenders paid	(541,725)	(400,536)	(141,189)	35.3%
Commissions paid	(5,135,536)	(3,865,703)	(1,269,833)	32.8%
Other underwriting, insurance and acquisition expenses paid	(3,679,616)	(3,386,407)	(293,209)	8.7%
Taxes paid	(518,966)	(210,551)	(308,415)	146.5%
Advances to mortgage loan originator	(2,466,020)	(555,685)	(1,910,335)	343.8%
Deposited policy applications unissued	2,220,132	1,613,015	607,117	37.6%
Decrease in short-term investment	549,851	541,655	8,196	1.5%
Other	(243,337)	(28,473)	(214,864)	754.6%
Increase in cash provided by operating activities	\$ 4,200,275	\$ 4,571,653	\$ (371,378)	-8.1%

Please see the statements of cash flows for the nine months ended September 30, 2016 and 2015 for a summary of the components of net cash used in investing activities and net cash provided by financing activities.

Our shareholders' equity as of September 30, 2016 and December 31, 2015 is summarized as follows:

	(Unaudited)		Amount Change 2016 less 2015	Percentage Change 2016 to 2015
	September 30, 2016	December 31, 2015		
Common stock, par value \$.01 per share (20,000,000 shares authorized, 8,050,173 issued as of September 30, 2016 and December 31, 2015 and 7,802,593 outstanding as of September 30, 2016 and December 31, 2015)	\$ 80,502	\$ 80,502	\$ -	0.0%
Additional paid-in capital	28,684,598	28,684,598	-	0.0%
Treasury stock, at cost (247,580 shares as of September 30, 2016 and December 31, 2015)	(893,947)	(893,947)	-	0.0%
Accumulated other comprehensive income (loss)	4,510,942	(2,655,817)	7,166,759	-269.9%
Accumulated earnings	6,131,705	4,999,707	1,131,998	22.6%
Total shareholders' equity	<u>\$ 38,513,800</u>	<u>\$ 30,215,043</u>	<u>\$ 8,298,757</u>	27.5%

The increase in shareholders' equity of \$8,298,757 for the nine months ended September 30, 2016 is due to \$7,166,759 of other comprehensive income and net income of \$1,131,998.

Equity per common share outstanding increased 27.6% from \$3.87 per share as of December 31, 2015 to \$4.94 per share as of September 30, 2016, based upon 7,802,593 common shares outstanding as of both September 30, 2016 and December 31, 2015.

The liquidity requirements of our life insurance companies are met primarily by funds provided from operations. Premium and annuity consideration deposits, investment income and investment maturities are the primary sources of funds, while investment purchases, policy benefits, and operating expenses are the primary uses of funds. There were no liquidity issues in 2016 or 2015. Fixed maturity securities amounting to \$134,592,061 as of September 30, 2016 are approximately 54% of our investments that are readily marketable and, if needed, could be converted to cash for liquidity needs.

We are subject to various market risks. The quality of our investment portfolio and the current level of shareholders' equity continue to provide a sound financial base as we strive to expand our marketing to offer competitive products.

Our investment portfolio had unrealized appreciation (depreciation) on available-for-sale securities of \$5,735,210 and (\$3,369,843) as of September 30, 2016 and December 31, 2015, respectively, prior to the impact of income taxes and deferred acquisition cost adjustments. An increase of \$9,440,894 in unrealized gains arising for the nine months ended September 30, 2016 includes 2016 net realized investment gains of \$335,841 originating from the sale and call activity for fixed maturity and equity securities available-for-sale resulting in a net increase in net unrealized appreciation for the nine months ended September 30, 2016 of \$9,105,053.

A primary liquidity concern is the risk of an extraordinary level of early policyholder withdrawals. We include provisions within our insurance policies, such as surrender charges, that help limit and discourage early withdrawals. Individual life insurance policies are less susceptible to withdrawal than annuity reserves and deposit liabilities because policyholders may incur surrender charges and undergo a new underwriting process in order to obtain a new insurance policy. Cash flow projections and cash flow tests under various market interest rate scenarios are also performed annually to assist in evaluating liquidity needs and adequacy. We currently anticipate that available liquidity sources and future cash flows will be adequate to meet our needs for funds.

One of our significant risks relates to the fluctuations in interest rates. Regarding interest rates, the value of our available-for-sale fixed maturity securities investment portfolio will increase or decrease in an inverse relationship with fluctuations in interest rates, while net investment income earned on newly acquired available-for-sale fixed maturity securities increases or decreases in direct relationship with interest rate changes. From an income perspective, we are exposed to rising interest rates which could be a significant risk, as TLIC's and FBLIC's annuity business is impacted by changes in interest rates. Life insurance company policy liabilities bear fixed rates. From a liquidity perspective, our fixed rate policy liabilities are relatively insensitive to interest rate fluctuations.

We believe gradual increases in interest rates do not present a significant liquidity exposure for the life insurance policies and annuity contracts. We maintain conservative durations in our fixed maturity portfolio. As of September 30, 2016, cash and cash equivalents, short-term investments, the fair value of fixed maturity available-for-sale securities with maturities of less than one year and the fair value of lottery receivables with maturities of less than one year equaled 14.9% of total policy liabilities. If interest rates rise significantly in a short time frame, 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.

In addition to the measures described above, TLIC and FBLIC must comply with the National Association of Insurance Commissioners promulgated Standard Valuation Law ("SVL") which specifies minimum reserve levels and prescribes methods for determining them, with the intent of enhancing solvency. Upon meeting certain tests, which TLIC and FBLIC met during 2015, the SVL also requires the Company to perform annual cash flow testing for TLIC and FBLIC. 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.

Our 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. We believe that our current liquidity, current bond portfolio maturity distribution and cash position give us substantial resources to administer our existing business and fund growth generated by direct sales.

The operations of TLIC and FBLIC may require additional capital contributions to meet statutory capital and surplus requirements mandated by state insurance departments. Life insurance contract liabilities are generally long term in nature and are generally paid from future cash flows or existing assets and reserves. We will service other expenses and commitments by: (1) using available cash, (2) dividends from TLIC and FBLIC that are limited by law to the greater of prior year net operating income or 10% of prior year-end surplus unless specifically approved by the controlling insurance department, (3) public and private offerings of our common stock and (4) corporate borrowings, if necessary.

We are not aware of any commitments or unusual events that could materially affect our capital resources. We are not aware of any current recommendations by any regulatory authority which, if implemented, would have a material adverse effect on our liquidity, capital resources or operations. We believe that our existing cash and cash equivalents as of September 30, 2016 will be sufficient to fund our anticipated operating expenses.

## Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements.

## SPECIAL NOTE CONCERNING FORWARD-LOOKING STATEMENTS

Certain statements contained herein are forward-looking statements. The forward-looking statements are made pursuant to the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995, and include estimates and assumptions related to economic, competitive and legislative developments. Forward-looking statements may be identified by words such as “expects,” “intends,” “anticipates,” “plans,” “believes,” “estimates,” “will” or words of similar meaning; and include, but are not limited to, statements regarding the outlook of our business and financial performance. These forward-looking statements are subject to change and uncertainty, which are, in many instances, beyond our control and have been made based upon our expectations and beliefs concerning future developments and their potential effect upon us. There can be no assurance that future developments will be in accordance with our expectations, or that the effect of future developments on us will be as anticipated. These forward-looking statements are not a guarantee of future performance and involve risks and uncertainties. There are certain important factors that could cause actual results to differ, possibly materially, from expectations or estimates reflected in such forward-looking statements. These factors include among others:

- general economic conditions and financial factors, including the performance and fluctuations of fixed income, equity, real estate, credit capital and other financial markets;
- differences between actual experience regarding mortality, morbidity, persistency, surrenders, investment returns, and our pricing assumptions establishing liabilities and reserves or for other purposes;
- the effect of increased claims activity from natural or man-made catastrophes, pandemic disease, or other events resulting in catastrophic loss of life;
- adverse determinations in litigation or regulatory matters and our exposure to contingent liabilities, including and in connection with our divestiture or winding down of businesses such as FTCC;
- inherent uncertainties in the determination of investment allowances and impairments and in the determination of the valuation allowance on the deferred income tax asset;
- investment losses and defaults;
- competition in our product lines;
- attraction and retention of qualified employees and agents;
- ineffectiveness of risk management policies and procedures in identifying, monitoring and managing risks;
- the availability, affordability and adequacy of reinsurance protection;
- the effects of emerging claim and coverage issues;
- the cyclical nature of the insurance business;
- interest rate fluctuations;
- changes in our experiences related to deferred policy acquisition costs;
- the ability and willingness of counterparties to our reinsurance arrangements and derivative instruments to pay balances due to us;
- impact of medical epidemics and viruses;
- domestic or international military actions;
- the effects of extensive government regulation of the insurance industry;
- changes in tax and securities law;
- changes in statutory or U.S. generally accepted accounting principles (“GAAP”), practices or policies;
- regulatory or legislative changes or developments;
- the effects of unanticipated events on our disaster recovery and business continuity planning;
- failures or limitations of our computer, data security and administration systems;
- risks of employee error or misconduct;
- the assimilation of life insurance businesses we acquire and the sound management of these businesses; and
- the availability of capital to expand our business.

It is not our corporate policy to make specific projections relating to future earnings, and we do not endorse any projections regarding future performance made by others. In addition, we do not publicly update or revise forward-looking statements based on the outcome of various foreseeable or unforeseeable developments.

## **Item 4. Controls and Procedures**

### **Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer (“Certifying Officers”), has evaluated the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities and Exchange Act of 1934 as amended (“Exchange Act”) as of the end of the fiscal period covered by this Quarterly Report on Form 10-Q. Based upon such evaluation, the Certifying Officers have concluded that the Company’s disclosure controls and procedures were effective to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is made known to management, including our Certifying Officers, as appropriate, to allow timely decisions regarding disclosure and that such information is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms.

### **Changes to Internal Control over Financial Reporting**

There were no changes in the Company’s internal control over financial reporting during the three months ended September 30, 2016 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

## **PART II - OTHER INFORMATION**

### **Item 1. Legal Proceedings**

The Company and Chairman, President and Chief Executive Officer, Gregg E. Zahn, filed an action in the District Court of Tulsa County, Oklahoma in 2013, Case No. CJ-2013-03385, against former Company Board of Directors member, Wayne Pettigrew and Mr. Pettigrew’s company, Group & Pension Planners, Inc. (the “Defendants”). The petition filed in the case alleges that Mr. Pettigrew, during and after the time he was a member of the Company’s Board of Directors, made defamatory statements regarding the Company and Mr. Zahn and committed breaches of his fiduciary duties to the Company. The defendants are alleged to have made defamatory statements to certain shareholders of the Company, to the press and to the Oklahoma Insurance Department and the Oklahoma Department of Securities. Mr. Pettigrew has denied the allegations.

The Board of Directors, represented by independent counsel, concluded that there was no action to be taken against Mr. Zahn and that the allegations by Mr. Pettigrew were without substance. The Company has been informed by the Oklahoma Insurance Department that it would take no action and also informed that the Oklahoma Department of Securities, after its investigation of the allegations, concluded that no proceedings were needed with respect to the alleged matters.

It is the Company’s intention to vigorously prosecute this action against the Defendants for damages and for the correction of the defamatory statements. In the opinion of the Company’s management, the ultimate resolution of any contingencies that may arise from this litigation is not considered material in relation to the financial position or results of operations of the Company.

Prior to its acquisition by TLIC, FBLIC developed, marketed, and sold life insurance products known as “Decreasing Term to 95” policies. On January 17, 2013, FBLIC’s Board of Directors voted that, effective March 1, 2013, it was not approving, and therefore was not providing, a dividend for the Decreasing Term to 95 policies. On November 22, 2013, three individuals who owned Decreasing Term to 95 policies filed a Petition in the Circuit Court of Greene County, Missouri asserting claims against FBLIC relating to FBLIC’s decision to not provide a dividend under the Decreasing Term to 95 policies.

On June 18, 2015, plaintiffs filed an amended petition. Like the original Petition, the amended Petition asserts claims for breach of contract and anticipatory breach of contract, and alleges that FBLIC breached, and will anticipatorily breach, the Decreasing Term to 95 policies of insurance by not providing a dividend sufficient to purchase a one year term life insurance policy which would keep the death benefit under the Decreasing Term to 95 policies the same as that provided during the first year of coverage under the policy.

It also asserts claims for negligent misrepresentation, fraud, and violation of the Missouri Merchandising Practices Act (“MMPA”). It alleges that during its sale of the Decreasing Term to 95 policies, FBLIC represented that the owners of these policies would always be entitled to dividends to purchase a one-year term life insurance policy and that the owners would have a level death benefit without an increase in premium.

The main difference between the original Petition and the amended Petition is that the amended Petition also seeks equitable relief based on two new theories: that the Decreasing Term to 95 policies should be reformed so that they will provide a level death benefit for a level premium payment until the policyholder reaches 95 years of age; and alternatively, Count VIII of the amended Petition asks the Court to (1) find that the dividend provisions in the Decreasing Term to 95 policies violate Missouri law, specifically, § 376.360 RSMo.; (2) order that the policies are *void ab initio*; and (3) order that FBLIC return all premiums collected under these policies. In addition, as part of the MMPA claim, plaintiffs are now alleging that FBLIC undertook a fraudulent scheme to sell the Decreasing Term to 95 policies as a level premium for level benefit even though FBLIC never intended to pay dividends for the life of the policies and that part of this alleged fraudulent scheme included having a dividend option which is not allowed under Missouri law.

FBLIC denies the allegations in the amended Petition and will continue to defend against them.

On February 1, 2016, the plaintiffs asked that the Court certify the case as a class action. With their motion, Plaintiffs filed an affidavit from an actuary stating the opinion that FBLIC has collected at least \$2,548,939 in premiums on the Decreasing Term to 95 policies. This presumably is the amount that Plaintiffs will seek to be refunded to policyholders if the policies are declared void. FBLIC opposed the request for class certification. On July 21, 2016, the Court certified three classes to maintain the claims for breach of contract, anticipatory breach of contract, violation of the MMPA, reformation, and to void the Decreasing Term to 95 policies. On August 1, 2016, FBLIC filed a Petition for Leave to Appeal with the Missouri Court of Appeals, Southern District asking for permission to appeal the Court’s class certification. The Petition for Leave to Appeal was denied.

FBLIC intends to defend vigorously against the class and individual allegations. The Company is unable to determine the potential magnitude of the claims in the event of a final certification and the plaintiffs prevailing on this substantive action.

On May 13, 2015, FBLIC filed a Counterclaim against Doyle Nimmo seeking indemnity and seeking damages for breach of fiduciary duty in the event FBLIC is liable under Plaintiffs’ underlying claims. In addition, on April 29, 2015, TLIC filed a lawsuit against Doyle Nimmo and Michael Teel alleging that they were liable for violations of federal and state securities laws for failing to disclose information relating to the Decreasing Term to 95 policies. This lawsuit is currently pending in the District Court for the Western District of Missouri (hereinafter the “Federal Lawsuit”). No claims have been made against TLIC in the Federal Lawsuit. The Federal Lawsuit has been stayed pending resolution of the lawsuit against FBLIC in the Circuit Court of Greene County, Missouri.

On September 28, 2015, Doyle Nimmo filed a Third-Party Petition for Declaratory Judgment (and Other Relief) against FBLIC. In this Third-Party Petition, Doyle Nimmo, a former director for FBLIC, seeks a declaratory judgment that the corporate by-laws of FBLIC require FBLIC to indemnify him for attorney’s fees, judgments, costs, fines, and amounts paid in defense of both the Counterclaim and the Federal Lawsuit and seeks a monetary judgment for the amounts expended by Doyle Nimmo in such defense. Prior to Doyle Nimmo’s filing of the Third-Party Petition, FBLIC’s Board of Directors executed a Unanimous Written Consent in Lieu of a Special Meeting in which it denied Doyle Nimmo’s tender of defense and request for indemnification finding Mr. Nimmo did not meet the applicable standard of conduct for indemnification under Missouri law. FBLIC intends to vigorously defend the Third-Party Petition on these grounds. The Company is unable to determine the potential magnitude of the claims in the event Doyle Nimmo prevails on his Third-Party Petition.

As stated above, FBLIC filed a Counterclaim and TLIC filed the Federal Lawsuit against Doyle Nimmo. Doyle Nimmo submitted a claim and tendered the defense of these claims to Utica Mutual Insurance Company under a policy providing Insurance Agents and Brokers Errors and Omissions Liability coverage. On November 4, 2015, Utica Mutual Insurance Company filed a lawsuit against Doyle Nimmo and other interested parties, including FBLIC and TLIC. The lawsuit is pending in the District Court for the Western District of Missouri and asks the Court to determine whether the Errors and Omissions policy provides coverage for the lawsuits filed against Doyle Nimmo. Utica Mutual Insurance Company does not seek a monetary judgment against FBLIC or TLIC.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

None

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. Mine Safety Disclosures**

None

**Item 5. Other Information**

None

**Item 6. Exhibits**

31.1 Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer

31.2 Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer

32.1 Section 1350 Certification of Principal Executive Officer

32.2 Section 1350 Certification of Principal Financial Officer

101.INS\*\* XBRL Instance

101.SCH\*\* XBRL Taxonomy Extension Schema

101.CAL\*\* XBRL Taxonomy Extension Calculation

101.DEF\*\* XBRL Taxonomy Extension Definition

101.LAB\*\* XBRL Taxonomy Extension Labels

101.PRE\*\* XBRL Taxonomy Extension Presentation

\*\*XBRL Information is furnished and not filed as part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise is not subject to liability under these sections.

## SIGNATURES

In accordance with requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

FIRST TRINITY FINANCIAL CORPORATION  
an Oklahoma corporation

November 10, 2016

By: /s/ Gregg E. Zahn  
Gregg E. Zahn, President and Chief Executive Officer

November 10, 2016

By: /s/ Jeffrey J. Wood  
Jeffrey J. Wood, Chief Financial Officer

CERTIFICATION

I, Gregg E. Zahn, Chief Executive Officer, certify that:

1. I have reviewed this Quarterly report on Form 10-Q of First Trinity Financial Corporation;
2. Based on my knowledge, this 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 report;
3. Based on my knowledge, the financial statements, and other financial information included in this 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 report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant, and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter, the registrant's fourth quarter in the case of an annual report, that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 10, 2016

By: /s/ Gregg E. Zahn  
Gregg E. Zahn, President and Chief Executive Officer



CERTIFICATION

I, Jeffrey J. Wood, Chief Financial Officer and Chief Accounting Officer, certify that:

1. I have reviewed this Quarterly report on Form 10-Q of First Trinity Financial Corporation;
2. Based on my knowledge, this 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 report;
3. Based on my knowledge, the financial statements, and other financial information included in this 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 report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant, and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, 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 report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter, the registrant's fourth quarter in the case of an annual report, that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 10, 2016

By: /s/ Jeffrey J. Wood  
Jeffrey J. Wood, Chief Financial Officer

EXHIBIT NO. 32.1

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. ss. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of First Trinity Financial Corporation, an Oklahoma corporation (the "Company"), hereby certifies that:

To my knowledge, the Quarterly Report on Form 10-Q of the Company for the quarter ended September 30, 2016 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 10, 2016

By: By: /s/ Gregg E. Zahn  
Gregg E. Zahn, President and Chief Executive Officer

EXHIBIT NO. 32.2

Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. ss. 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of First Trinity Financial Corporation, an Oklahoma corporation (the "Company"), hereby certifies that:

To my knowledge, the Quarterly Report on Form 10-Q of the Company for the quarter ended September 30, 2016 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 10, 2016

by: /s/ Jeffrey J. Wood  
Jeffrey J. Wood, Chief Financial Officer