UNITED STATES CELLULAR CORP
Form 15-12B
January 04, 2010

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 15

Certification and Notice of Termination of Registration under Section 12(g) of

the Securities Exchange Act of 1934 or Suspension of Duty to File Reports under

Sections 13 and 15(d) of the Securities Exchange Act of 1934

Commission File Number **001-09712**

United States Cellular Corporation

(Exact name of registrant as specified in its charter)

8410 W. Bryn Mawr Ave., Chicago, IL 60631, 773-399-8900

(Address, including zip code, and telephone number, including

area code, of registrant s principal executive offices)

8.75% Senior Notes Due 2032
(Title of each class of securities covered by this Form)

Common Shares, $1.00 par value
7.50% Senior Notes due 2034
(Titles of all other classes of securities for which a duty to file reports under section 13(a) or 15(d) remains)

Please place an X in the box(es) to designate the appropriate rule provision(s) relied upon to terminate or suspend the duty to file reports:

Rule 12g-4(a)(1)	¨
Rule 12g-4(a)(2)	¨
Rule 12h-3(b)(1)(i)	x
Rule 12h-3(b)(1)(ii)	¨
Rule 15d-6	x

Approximate number of holders of record as of the certification or notice date: **None**

Pursuant to the requirements of the Securities Exchange Act of 1934, United States Cellular Corporation has caused this certification/notice to be signed on its behalf by the undersigned duly authorized person.

United States Cellular Corporation

DATE: **January 4, 2010**

By: /s/ Kenneth R. Meyers
Kenneth R. Meyers

Chief Accounting Officer

FAMILY: times new roman; FONT-SIZE: 10pt"> 66,004 60,690
BENEFITS AND EXPENSES

Policyholder benefits paid or provided
35,839 44,746

Amortization of deferred policy acquisition costs
3,673 4,344

Commissions
7,863 8,262

General and administrative expenses
10,396 8,558

Taxes, licenses and fees
1,631 1,447

Interest expense
1,126 1,147 60,528 68,504

Income (Loss) Before Income Tax Expense (Benefit)
5,476 (7,814)

INCOME TAX EXPENSE (BENEFIT)

Current
1,136 (3,495)

Deferred
116 885 1,252 (2,610)
Net Income(Loss)
$4,224 $(5,204)

Net Earnings (Loss) Per Common Share
$1.71 $(2.11)

See accompanying notes to consolidated financial statements

THE NATIONAL SECURITY GROUP, INC.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Dollars in thousands)

	Total	Comprehensive Income (Loss)	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Common Stock	Paid-in Capital
Balance at December 31, 2007	$ 48,447	$ -	$ 36,165	$ 4,864	$ 2,467	$ 4,951
Comprehensive loss:						
Net loss for 2008	(5,204)	(5,204)	(5,204)	-	-	-
Other comprehensive loss, net of tax						
Unrealized loss on securities, net of reclassification adjustment of ($978)	(6,147)	(6,147)	-	(6,147)	-	-
Unrealized loss on interest rate swap	(228)	(228)	-	(228)	-	-
Comprehensive loss		(11,579)				
Cash dividends ($0.90 per share)	(2,220)		(2,220)	-	-	-
Balance at December 31, 2008	34,648		28,741	(1,511)	2,467	4,951
Comprehensive income:						
Net income for 2009	4,224	4,224	4,224	-	-	-
Other comprehensive income, net of						

tax						
Unrealized gain on securities, net of reclassification adjustment of $282	3,520	3,520	-	3,520	-	-
Unrealized gain on interest rate swap	256	256	-	256	-	-
Comprehensive income		8,000				
Cash dividends ($0.60 per share)	(1,480)		(1,480)	-	-	-
Balance at December 31, 2009	$ 41,168		$ 31,485	$ 2,265	$ 2,467	$ 4,951

See accompanying notes to consolidated financial statements.

48

The National Security Group, Inc.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	(Dollars in thousands) Year ended December 31,	
	2009	2008
Cash flows from operating activities:		
Net income (loss)	$ 4,224	$ (5,204)
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation expense and amortization/accretion, net	229	409
Increase in cash surrender of company owned life insurance	(740)	543
Net realized (gains) losses on investments	(357)	1,049
Deferred income taxes	116	(885)
Amortization of deferred policy acquisition costs	3,673	4,344
Changes in assets and liabilities:		
Change in receivable for securities	417	(513)
Change in accrued investment income	2	(10)
Change in reinsurance recoverable	3,362	(3,229)
Policy acquisition costs deferred	(4,058)	(5,176)
Change in accrued income taxes	2,432	(3,400)
Change in prepaid reinsurance premiums	(10)	(2)
Change in net policy liabilities and claims	(1,738)	8,105
Change in other liabilities	1,284	(2,204)
Other, net	(113)	281
Net cash provided by (used in) operating activities	8,723	(5,892)
Cash flows from investing activities:		
Purchases of:		
Available-for-sale securities	(30,594)	(22,514)
Trading securities and short-term investments	(141)	(154)
Real estate held for investment	(66)	(446)
Company owned life insurance	(2,500)	(2,500)
Other invested assets	(108)	(3,714)
Property and equipment	(116)	(368)
Proceeds from sale or maturities of:		
Held-to-maturity securities	4,926	6,377
Available-for-sale securities	22,830	28,938
	20	1,165

Trading securities and short-term investments				
Real estate held for investment		19		720
Other invested assets		732		1,259
Other		(589)		(58)
Net cash (used in) provided by investing activities		(5,587)		8,705
Cash flows from financing activities:				
(Repayment of) Proceeds from short-term debt		-		(900)
Change in other policyholder funds		3		35
Dividends paid		(1,480)		(2,220)
Net cash used in financing activities		(1,477)		(3,085)
Net increase (decrease) in cash		1,659		(272)
Cash at beginning of year		3,027		3,299
Cash at end of year	$	4,686	$	3,027

See accompanying notes to consolidated financial statements.

49

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Basis of Presentation
The accompanying consolidated financial statements include the accounts of The National Security Group, Inc. (the Company) and its wholly-owned subsidiaries: National Security Insurance Company (NSIC), National Security Fire and Casualty Company (NSFC) and NATSCO, Inc. (NATSCO). NSFC includes a wholly-owned subsidiary - Omega One Insurance Company (Omega) . The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). All significant intercompany transactions and accounts have been eliminated.

The significant accounting policies followed by the Company and subsidiaries that materially affect financial reporting are summarized below.

Description of Business
NSIC is licensed in the states of Alabama, Florida, Georgia, Mississippi, South Carolina and Texas and was organized in 1947 to provide life and burial insurance policies to the home service market. Business is now produced by both company and independent agents. Primary products include ordinary life, accident and health, supplemental hospital, and cancer insurance products.

NSFC is licensed in Alabama, Arkansas, Florida, Georgia, Kentucky, Mississippi, Oklahoma, South Carolina, Tennessee and West Virginia. In addition, NSFC operates on a surplus lines basis in Louisiana, Missouri, and Texas. NSFC operates in various property and casualty lines, the most significant of which are dwelling property fire and extended coverage, homeowners, mobile homeowners, ocean marine, private passenger automobile physical damage and liability and commercial auto liability.

Omega is licensed in the states of Alabama and Louisiana. Omega operates in property and casualty lines, the most significant of which are homeowners and private passenger automobile physical damage and liability.

The Company is incorporated under the laws of the State of Delaware. Its Common Stock is traded on the NASDAQ Global Market under the ticker symbol NSEC. Pursuant to the regulations of the United States Securities and Exchange Commission (SEC), the Company is considered a "Smaller Reporting Company" as defined by SEC Rule 12b-2 of the Exchange Act. The Company has elected to comply with the new scaled disclosure requirements of Regulation S-K and only two years of financial statements are included herein. The Company previously used a non-accelerated filer status.

Use of Estimates
The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Among the more significant estimates included in these financial statements are reserves for future policy benefits, liabilities for losses and loss adjustment expenses, reinsurance recoverable asset on associated loss and loss adjustment expense liabilities, deferred policy acquisition costs, deferred income tax assets and liabilities, and assessments of other than temporary impairments on investments. Actual results could differ from those estimates.

Concentration of Risk
The Company's property and casualty segment is licensed or operates on a surplus lines basis in 13 states. However, over 60% of segment revenue is generated in the states of Alabama, Mississippi and Louisiana, subjecting the Company to significant geographic concentration. Consequently, adverse weather conditions or changes in the legal,

regulatory or economic environment could adversely impact the Company.

The Company's life, accident and health insurance segment, composing nearly 12% of consolidated revenues, is licensed in six states. However, over 75% of segment revenue is generated in the states of Alabama and Georgia. Consequently, changes in the legal, regulatory or economic environment could adversely impact the Company.

For the year ended December 31, 2009 and 2008, there was one agency in the property and casualty segment that individually produced greater than 5% of the Company's direct written premium.

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Investments
The Company's securities are classified as follows:

- Securities Held-to-Maturity. Bonds, notes and redeemable preferred stock for which the Company has the positive intent and ability to hold to maturity are reported at cost, adjusted for amortization of premiums and accretion of discounts which are recognized in interest income using methods which approximate level yields over the period to maturity.

- Securities Available-for-Sale. Bonds, notes, common stock and non-redeemable preferred stock not classified as either held-to-maturity, or trading are reported at fair value, and adjusted for other-than-temporary declines in fair value.

- Trading Securities. Trading securities are classified as such on the balance sheet and reported at fair value.

Unrealized gains and losses on investments, net of tax, on securities available-for-sale are reflected directly in shareholders' equity as a component of accumulated other comprehensive income, and accordingly, have no effect on net income until realized.

Changes in fair value of trading securities are recognized in net income.

Realized gains and losses on the sale of investments available-for-sale are determined using the specific-identification method and include write downs on available-for-sale investments considered to have other than temporary declines in market value.

When a fixed maturity security has a decline in value, where fair value is below amortized cost, an other-than-temporary impairment (OTTI) is triggered in circumstances where:

- the Company has the intent to sell the security

- it is more likely-than-not that the Company will be required to sell the security before recovery of its amortized cost basis

- the Company does not expect to recover the entire amortized cost basis of the security.

If the Company intends to sell the security or if it is more-likely-than not the Company will be required to sell the security before recovery, an OTTI is recognized as a realized loss in the income statement equal to the difference between the security's amortized cost and its fair value. If the Company does not intend to sell the security or it is not more-likely-than not that the Company will be required to sell the security before recovery, the OTTI is separated into an amount representing the credit loss, which is recognized as a realized loss in the income statement, and the amount related to all other factors, which is recognized in other comprehensive income.

When an equity security has a decline in value, where fair value is below cost, that is deemed to be other than temporary, the Company reduces the book value of the security to its current fair value, recognizing the decline as a realized loss in the income statement. Any future increases in the market value of investments written down are reflected as changes in unrealized gains as part of accumulated other comprehensive income within stockholders' equity.

Interest on fixed income securities is credited to income as it accrues on the principal amounts outstanding adjusted for amortization of premiums and accretion of discounts computed utilizing the effective interest rate method. Premiums and discounts on mortgage backed securities are amortized or accreted using anticipated prepayments with changes in anticipated prepayments accounted for prospectively. The model used to determine anticipated prepayment assumptions for mortgage backed securities uses separate home sale, refinancing, curtailment and pay-off assumptions derived from a variety of industry sources. Mortgage-backed security valuations are subject to prospective adjustments in yield due to changes in prepayment assumptions. The utilization of the prospective method will result in a recalculated effective yield that will equate the carrying amount of the investment to the present value of the projected future cash flows. The recalculated yield is used to accrue income on investments for subsequent periods.

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Mortgage loans and policy loans are stated at the unpaid principal balance of such loans.

Investment real estate is reported at cost, less allowances for depreciation computed on the straight-line basis. Investment real estate consists primarily of timberland and undeveloped commercial real estate. Real estate is carried at cost.

Other investments consist primarily of investments in notes and equity investments in limited liability companies and company owned life insurance. The Company has no influence or control over the operating or financial policies of the investee limited liability companies and consequently, these investments are accounted for using the cost method.

The Company owns life insurance contracts on certain management employees. The life insurance contracts are carried at their current cash surrender value. Changes in cash surrender values are included in income in the current period. Death proceeds from the contracts are recorded when the proceeds become payable under the terms of the policy.

Cash and short-term investments are carried at cost, which approximates market value.

Investments with other than temporary impairment in value are written down to estimated realizable values and losses recognized in the determination of net income. The fair value of the investment becomes its new cost basis.

Fair Values of Financial Instruments
The Company uses the following methods and assumptions to estimate fair values:

Investments – Fixed income security fair values are based on quoted market prices when available. If not available, fair values are based on values obtained from investment brokers and independent pricing services.

Equity security fair values are based on quoted market prices.

Multiple observable inputs are not available for certain of our investments, primarily private placements and limited partnerships. Management values these investments either using non-binding broker quotes or pricing models that utilize market based assumptions that have limited observable inputs.

Receivables and reinsurance recoverable – The carrying amounts reported approximate fair value.

Interest rate swaps – The estimated fair value of the interest rate swaps is based on valuations received from financial institution counterparties.

Trust preferred securities obligations and line of credit obligations – The carrying amounts reported for these instruments are equal to the principal balance outstanding and approximate their fair value.

Policy Receivables
Receivable balances are reported at unpaid balances, less a provision for credit losses.

Accounts Receivable
Accounts receivable are reported at net realizable value. Management determines the allowance for doubtful accounts based on historical losses and current economic conditions. On a continuing basis, management analyzes delinquent receivables and, once these receivables are determined to be uncollectible, they are written off through a charge

against an existing allowance account or against earnings.

Property and Equipment

Property and equipment is carried at cost less accumulated depreciation and includes expenditures that substantially increase the useful lives of existing property and equipment. Significant costs incurred for internally developed software are capitalized and amortized over estimated useful lives of 3 years. Maintenance, repairs, and minor renovations are charged to expense as incurred. Upon sale or retirement of property and equipment, the costs and related accumulated depreciation are eliminated from the respective account and the resulting gain or loss is included in the results of operations. The Company provides for depreciation of property and equipment using the straight-line method designed to amortize costs over estimated useful lives. Estimated useful lives range up to 40 years for buildings and from 3-8 years

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

for electronic data processing equipment and furniture and fixtures. Property and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

Statement of Cash Flows
For purposes of reporting cash flows, cash includes cash-on-hand, demand deposits with banks and overnight investments.

Premium Revenue
Life insurance premiums are recognized as revenues when due. Property and casualty insurance premiums include direct writings plus reinsurance assumed less reinsurance ceded and are recognized on a pro rata basis over the terms of the policies. Unearned premiums represent that portion of direct premiums written that are applicable to the unexpired terms of policies in force and is reported as a liability. Prepaid reinsurance premiums represent the unexpired portion of premiums ceded to reinsurers and is reported as an asset.

Deferred Policy Acquisition Costs
The costs of acquiring new insurance business are deferred and amortized over the lives of the policies. Deferred costs include commissions, premium taxes, other agency compensation and expenses, and other underwriting expenses directly related to the level of new business produced.

Acquisition costs relating to life contracts are amortized over the premium paying period of the contracts, or the first renewal period of term policies, if earlier. Assumptions utilized in amortization are consistent with those utilized in computing policy liabilities.

The method of computing the deferred policy acquisition costs for property and casualty policies limits the amount deferred to a percentage of related unearned premiums.

Policy Liabilities
The liability for future life insurance policy benefits is computed using a net level premium method including the following assumptions:

Years of Issue	Interest Rate
1947 - 1968	4%
1969 - 1978	6% graded to 5%
1979 - 2003	7% graded to 6%
2004 - 2009	5.25%

Mortality assumptions include various percentages of the 1955-60 and 1965-70 Select and Ultimate Basic Male Mortality Table. Withdrawal assumptions are based on the Company's experience.

Claim Liabilities
The liability for unpaid claims represents the estimated liability for claims reported to the Company and its subsidiaries plus claims incurred but not yet reported and the related loss adjustment expenses. The liabilities for claims and related adjustment expenses are determined using case-basis evaluations and statistical analyses and represent estimates of the ultimate net cost of all losses incurred through December 31 of each year. Although considerable variability is inherent in such estimates, management believes that the liabilities for unpaid claims and related loss adjustment expenses are adequate. The estimates are continually reviewed and adjusted as necessary; such adjustments are included in the period in which they are determined.

Earnings Per Share

Earnings per share of common stock is based on the weighted average number of shares outstanding during each year. The adjusted weighted average shares outstanding were 2,466,600 (2,466,600 in 2008).

Reinsurance

In the normal course of business, NSFC seeks to reduce the loss that may arise from catastrophes or other events that cause unfavorable underwriting results by reinsuring certain levels of risk in various areas of exposure with other insurance enterprises or reinsurers. In 2009, NSFC maintained a catastrophe reinsurance agreement to cover losses from catastrophic events, primarily hurricanes.

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Under the catastrophe reinsurance program, the Company retains the first $3.5 million in losses from each event. Reinsurance is maintained in four layers as follows:

Layer	Reinsurers' Limits of Liability
First Layer	95% of $6,500,000 in excess of $3,500,000
Second Layer	95% of $7,500,000 in excess of $10,000,000
Third Layer	100% of $25,000,000 in excess of $17,500,000
Fourth Layer	100% of $30,000,000 in excess of $42,500,000

Layers 1-3 cover events occurring from January1-December 31 of the contract year. The Company placed the fourth layer in July allowing an interim review of exposure and projected storm patterns for the current contract year. The fourth layer covers events occurring from July 1-June 30 of the contract year. All significant reinsurers under the program carry A.M. Best ratings of A- (Excellent) or higher.

Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Amounts paid for prospective reinsurance contracts are reported as prepaid reinsurance premiums and amortized over the remaining contract period.

In the normal course of business, NSIC seeks to limit its exposure to loss on any single insured and to recover a portion of benefits paid by ceding reinsurance to other insurance enterprises or reinsurers under excess coverage contracts. NSIC retains a maximum of $50,000 of coverage per individual life. The cost of reinsurance is amortized over the contract period of the reinsurance.

Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Deferred income taxes arise from the recognition of temporary differences between financial statement carrying amounts and the tax bases of the Company’s assets and liabilities and operating loss carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is provided when it is more likely than not that some portion of the deferred tax asset will not be realized. The effect of a change in tax rates is recognized in the period the new rate is enacted.

The Company evaluates all tax positions taken on its U.S. federal income tax return. No material uncertainties exist for any tax positions taken by the Company

Contingencies

Liabilities for loss contingencies arising from, but not limited to, litigation, claims, assessments, fines and penalties are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

Reclassifications

Certain 2008 amounts have been reclassified from the prior year financial statements to conform to the 2009 presentation.

Advertising

The Company expenses advertising costs as incurred. Advertising costs charged to expense were $109,000 for the year ended December 31, 2009 ($186,000 for the year ended December 31, 2008). Advertising cost consists primarily of agent convention expense and print media.

Concentration of Credit Risk

The Company maintains cash depository accounts which, at times, may exceed federally insured limits. These amounts represent actual account balances held by financial institutions at the end of the period, and unlike the balance reported in the financial statements, the account balances do not reflect timing delays inherent in reconciling items such as outstanding checks and deposits in transit. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

Policy receivables are reported at unpaid balances. Policy receivables are generally offset by associated unearned premium liabilities and are not subject to significant credit risk. Receivables from agents, less provision for credit losses, are composed of balances due from independent agents. At December 31, 2009 the single largest balance due from one agent totaled $525,000.

Reinsurance contracts do not relieve the Company of its obligations to policyholders. A failure of a reinsurer to meet their obligation could result in losses to the insurance subsidiaries. Allowances for losses are established if amounts are believed to be uncollectible. At December 31, 2009 and 2008, no amounts were deemed uncollectible. The Company, at least annually, evaluates the financial condition of all reinsurers and evaluates any potential concentrations of credit risk. At December 31, 2009, management does not believe the Company is exposed to any significant credit risk related to its reinsurance program.

Recently Issued Accounting Standards

In April 2009, a new accounting standard was issued which amends the recognition guidance for other-than-temporary impairments (OTTI) of debt securities and expands the financial statement disclosures for OTTI on debt and equity securities.

- This new accounting standard states that an OTTI write-down of debt securities, where fair value is below amortized cost, is triggered in circumstances where (1) an entity has the intent to sell a security, (2) it is more-likely-than-not that the entity will be required to sell the security before recovery of its amortized cost basis, or (3) the entity does not expect to recover the entire amortized cost basis of the security. If an entity intends to sell a security or if it is more-likely-than-not the entity will be required to sell the security before recovery, an OTTI write-down is recognized in earnings equal to the difference between the security’s amortized cost and its fair value. If an entity does not intend to sell the security or it is not more-likely-than-not that it will be required to sell the security before recovery, the OTTI write-down is separated into an amount representing the credit loss, which is recognized in earnings, and the amount related to all other factors, which is recognized in other comprehensive income.

- This new accounting standard requires that companies record, as of the beginning of the interim period of adoption, a cumulative-effect adjustment to reclassify the noncredit component of a previously recognized OTTI loss from retained earnings to other comprehensive income if the Company does not intend to sell the security and it is more-likely-than-not that the Company will not be required to sell the security before recovery of its amortized cost basis. The adoption had no impact on our financial position or results of operations. The Company had no cumulative-effect adjustment upon adoption at the beginning of the second quarter.

In April 2009, a new accounting standard was issued related to determining fair value when the volume and level of activity for the asset or liability have significantly decreased and identifying transactions that are not orderly. Our adoption of this new accounting standard was effective April 1, 2009. The new accounting standard reaffirms that fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. The new accounting standard also reaffirms the need to use judgment in determining if a formerly active market has become inactive and in determining fair values when the market has become inactive. The implementation of the new guidance did not have a significant impact on our financial statements.

In April 2009, a new accounting standard was issued related to interim disclosures about fair value of financial instruments. The new accounting standard requires disclosing qualitative and quantitative information about the fair value of all financial instruments on a quarterly basis, including methods and significant assumptions used to estimate fair value during the period. These disclosures were previously only done annually. The disclosures required by the new accounting standard were effective for the quarter ending June 30, 2009. The implementation of the new guidance did not have a significant impact on our financial statements.

In June 2009, a new accounting standard was issued related to the accounting for transfers of financial assets, which updates accounting for securitizations and special-purpose entities. The new accounting standard is a revision of previously issued accounting standards related to accounting for transfers and servicing of financial assets and extinguishments of liabilities, and will require additional information regarding financial asset transfers, including

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES – CONTINUED

securitization transactions, and the presence of continuing exposure around the risks related to transferred financial assets. In addition, the new accounting standard removes the concept of a qualifying special-purpose entity and changes the requirements for de-recognizing financial assets. The new accounting standard was effective January 1, 2010. We do not expect the implementation of this new accounting standard to have a significant impact on our financial statements.

In June 2009, new consolidation guidance was issued which replaces the quantitative-based risks and rewards calculation for determining whether an enterprise is the primary beneficiary in a variable interest entity with an approach that is primarily qualitative, requires ongoing assessments whether an enterprise is the primary beneficiary of a variable interest entity, and requires additional disclosure about an enterprise's involvement in variable interest entities. This guidance is effective for financial statements issued for fiscal years beginning after November 15, 2009. We do not expect the adoption of this guidance to have a material impact on our financial statements.

Effective July 1, 2009, the Financial Accounting Standards Board (FASB) issued the Accounting Standards Codification (ASC), which combined and superseded all existing non-SEC accounting and reporting standards under GAAP and became the single official source for authoritative GAAP guidance combined with guidance issued by the U.S. Securities and Exchange Commission (SEC). The FASB no longer issues new standards in the previous formats. Instead, amendments to the Codification are made by issuing "Accounting Standards Updates" (ASU). The Codification did not change existing GAAP. Accordingly, the issuance of the codification did not impact the Company's consolidated results of operations or financial condition.

In August 2009, the FASB issued ASU 2009-05 "Measuring Liabilities at Fair Value" ("ASU 2009-05"). ASU 2009-05 updated ASC Section 820-10 ("Fair Value Measurements") to provide additional guidance on how to measure liabilities at fair value for which a quoted price in an active market is not available. In this situation a company can either use the quoted price of an identical liability when traded as an asset or the quoted price of similar liabilities when traded as assets. As of December 31, 2009, the only liability measured at fair value was an interest rate swap discussed in Note 7. The new guidance was effective for the company on October 1, 2009. The implementation of the new guidance did not have a significant impact on our financial statements.

NOTE 2 – VARIABLE INTEREST ENTITIES

The Company holds a passive interest in a limited partnership that is considered to be a Variable Interest Entity (VIE) under the provisions of FIN 46(R). The Company is not the primary beneficiary of the entity and is not required to consolidate under FIN 46(R). The entity is a private placement investment fund formed for the purpose of investing in private equity investments. The Company owns less than 1% of the limited partnership. The carrying value of the investment totals $325,000 and is included as a component of Other Invested Assets.

In December 2005, the Company formed National Security Capital Trust I, a statutory trust created under the Delaware Statutory Trust Act, for the sole purpose of issuing, in private placement transactions, $9,000,000 of trust preferred securities (TPS) and using the proceeds thereof, together with the equity proceeds received from the Company in the initial formation of the Trust, to purchase $9,300,000 of variable rate subordinated debentures issued by the Company. The Company owns all voting securities of the Trust and the subordinated debentures are the sole assets of the Trust. The Trust will meet the obligations of the TPS with the interest and principal paid on the subordinated debentures. The Company received net proceeds from the TPS transactions, after commissions and other costs of issuance, of $9,005,000. The Company also holds all the voting securities issued by the Trust and such trusts are considered to be VIE's. The Trust is not consolidated because the Company is not the primary beneficiary of the trust. The Subordinated Debentures, disclosed in Note 9, are reported in the accompanying Consolidated Balance

Sheets as a component of long-term debt. The Company's equity investments in the Trust total $279,000 and are included in Other Assets.

In June 2007, the Company formed National Security Capital Trust II for the sole purpose of issuing, in private placement transactions, $3,000,000 of trust preferred securities (TPS) and using the proceeds thereof, together with the equity proceeds received from the Company in the initial formation of the Trust, to purchase $3,093,000 unsecured junior subordinated deferrable interest debentures. The Company owns all voting securities of the Trust and the subordinated debentures are the sole assets of the Trust. The Trust will meet the obligations of the TPS with the interest and principal paid on the subordinated debentures. The Company received net proceeds from the TPS transactions, after commissions and other costs of issuance, of $2,995,000. The Company also holds all the voting securities issued by the Trust and such trusts are considered to be VIE's. The Trust is not consolidated because the Company is not the primary beneficiary of the Trust. The Subordinated Debentures, disclosed in Note 9, are reported in the accompanying Consolidated Balance

NOTE 2 – VARIABLE INTEREST ENTITIES – CONTINUED

Sheets as a component of long-term debt. The Company's equity investments in the Trust total $93,000 and are included in Other Assets.

NOTE 3 – STATUTORY ACCOUNTING PRACTICES

The accompanying consolidated financial statements have been prepared in conformity with generally accepted accounting principles (GAAP) which vary in certain respects from reporting practices prescribed or permitted by insurance regulatory authorities. The significant differences for statutory reporting include: (a) acquisition costs of acquiring new business are charged to operations as incurred, (b) life policy liabilities are established utilizing interest and mortality factors specified by regulatory authorities, (c) the Asset Valuation Reserve (AVR) and the Interest Maintenance Reserve (IMR) are recorded as liabilities, and (d) non-admitted assets (furniture and equipment, agents' debit balances and prepaid expenses) are charged directly to surplus.

Statutory net gains (losses) from operations and capital and surplus, excluding intercompany transactions, are summarized as follows:

	2009	2008
NSIC - including realized capital gains (losses) of $234 and $(1,509), respectively	$ 1,314	$ (442)
NSFC - including realized capital gains of $198 and $615, respectively	$ 4,179	$ (5,730)
Omega - including realized capital (losses) of $(78) and $(231), respectively	$ 246	$ (344)
Statutory risk-based adjusted capital:		
NSIC - including AVR of $517 and $191, respectively	$ 9,642	$ 8,396
NSFC	$ 28,742	$ 26,783
Omega	$ 9,568	$ 9,087

The above amounts exclude allocation of overhead from the Company. NSIC, NSFC and Omega are in compliance with statutory restrictions with regard to minimum amounts of surplus and capital.

NOTE 4 – INVESTMENT SECURITIES

The amortized cost and aggregate fair values of investments in securities are as follows:

	(Dollars in thousands)			
	December 31, 2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
Corporate debt securities	$ 26,786	$ 1,557	$ 519	$ 27,824
Mortgage backed securities	8,203	282	165	8,320
Private label mortgage backed securities	9,634	72	810	8,896
Obligations of states and political subdivisions	15,641	211	336	15,516
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	9,532	261	80	9,713
Total fixed maturities	69,796	2,383	1,910	70,269
Equity securities	5,851	3,990	806	9,035
Total	$ 75,647	$ 6,373	$ 2,716	$ 79,304
Held-to-maturity securities:				
Mortgage backed securities	$ 3,175	$ 101	$ 25	3,251
Private label mortgage backed securities	187	5	-	192
Obligations of states and political subdivisions	2,139	51	8	2,182
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	441	14	-	455
Total	$ 5,942	$ 171	$ 33	$ 6,080
	December 31, 2008			
		Gross	Gross	

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale securities:				
Corporate debt securities	$ 21,153	$ 84	$ 2,277	$ 18,960
Mortgage backed securities	11,101	257	24	11,334
Private label mortgage backed securities	6,590	2	1,369	5,223
Obligations of states and political subdivisions	13,401	81	875	12,607
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	9,551	433	1	9,983
Total fixed maturities	61,796	857	4,546	58,107
Equity securities	5,467	3,130	1,028	7,569
Total	$ 67,263	$ 3,987	$ 5,574	$ 65,676
Held-to-maturity securities:				
Corporate debt securities	$ 88	$ -	$ 3	$ 85
Mortgage backed securities	4,087	20	41	4,066
Private label mortgage backed securities	249	-	1	248
Obligations of states and political subdivisions	2,141	34	14	2,161
U.S. Treasury securities and obligations of U.S. Government corporations and agencies	4,387	48	-	4,435
Total	$ 10,952	$ 102	$ 59	$ 10,995

NOTE 4 – INVESTMENT SECURITIES – CONTINUED

The amortized cost and aggregate fair value of debt securities at December 31, 2009, by contractual maturity, are as follows. 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.

	(Dollars in Thousands)	
	Amortized	Fair
Available-for-sale securities:	Cost	Value
Due in one year or less	$ 419	$ 425
Due after one year through five years	14,320	15,551
Due after five years through ten years	24,013	24,433
Due after ten years	31,044	29,860
Total	$ 69,796	$ 70,269
Held-to-maturity securities:		
Due in one year or less	$ 303	$ 309
Due after one year through five years	802	828
Due after five years through ten years	1,929	1,991
Due after ten years	2,908	2,952
Total	$ 5,942	$ 6,080

A summary of securities available-for-sale with unrealized losses as of December 31, 2009 and 2008 along with the related fair value, aggregated by the length of time that investments have been in a continuous unrealized loss position, is as follows:

	(Dollars in thousands)					December 31, 2009	
	Less than 12 months		12 months or longer		Total		
		Gross		Gross		Gross	Total
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Securities in a Loss Position
Fixed maturities:	$ 1,856	$ 21	$ 6,772	$ 498	$ 8,628	$ 519	23

Corporate debt securities							
Mortgage backed securities	1,443	156	71	9	1,514	165	6
Private label mortgage backed securities	2,660	72	4,651	738	7,311	810	15
Obligations of state and political subdivisions	5,889	199	991	137	6,880	336	21
U.S. Treasury securities and obligations of U.S. government corporations and agencies	3,708	80	-	-	3,708	80	11
Equity securities	78	13	2,283	793	2,361	806	13
	$ 15,634	$ 541	$ 14,768	$ 2,175	$ 30,402	$ 2,716	89

59

NOTE 4 – INVESTMENT SECURITIES – CONTINUED

(Dollars in thousands)						December 31, 2008
	Less than 12 months		12 months or longer		Total		
		Gross		Gross		Gross	Total
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized	Securities in a
	Value	Losses	Value	Losses	Value	Losses	Loss Position
Fixed maturities:							
Corporate debt securities	$ 9,904	$ 1,337	$ 4,396	$ 940	$ 14,300	$ 2,277	45
Mortgage backed securities	315	5	1,868	19	2,183	24	9
Private label mortgage backed securities	412	87	4,354	1,282	4,766	1,369	11
Obligations of state and political subdivisions	3,745	332	4,812	543	8,557	875	25
U.S. Treasury securities and obligations of U.S. government corporations and agencies	295	1	-	-	295	1	1
Equity securities	981	446	731	582	1,712	1,028	12
	$ 15,652	$ 2,208	$ 16,161	$ 3,366	$ 31,813	$ 5,574	103

For 2009, gross gains of $1,102,000 ($2,070,000 for 2008) and gross losses of $319,000 ($611,000 for 2008) were realized on sales of available-for-sale-securities.

A summary of securities held-to-maturity with unrealized losses as of December 31, 2009 and 2008 along with the related fair value, aggregated by the length of time that investments have been in a continuous unrealized loss position, is as follows:

(Dollars in thousands)						December 31, 2009
Less than 12 months		12 months or longer		Total		
	Gross		Gross		Gross	Total
Fair	Unrealized	Fair	Unrealized	Fair	Unrealized	Securities in a

	Value	Losses	Value	Losses	Value	Losses	Loss Position
Fixed maturities:							
Corporate debt securities	$ -	$ -	$ -	$ -	$ -	$ -	-
Mortgage backed securities	-	-	333	25	333	25	2
Private label mortgage backed securities	-	-	-	-	-	-	-
Obligations of state and political subdivisions	160	4	351	4	511	8	2
U.S. Treasury securities and obligations of U.S. government corporations and agencies	-	-	-	-	-	-	-
	$ 160	$ 4	$ 684	$ 29	$ 844	$ 33	4

	(Dollars in thousands)					December 31, 2008	
	Less than 12 months		12 months or longer		Total		
		Gross		Gross		Gross	Total
	Fair	Unrealized	Fair	Unrealized	Fair	Unrealized	Securities in a
	Value	Losses	Value	Losses	Value	Losses	Loss Position
Fixed maturities:							
Corporate debt securities	$ 84	$ 3	$ -	$ -	$ 84	$ 3	1
Mortgage backed securities	-	-	2,408	41	2,408	41	7
Private label mortgage backed securities	249	1	-	-	249	1	1
Obligations of state and political subdivisions	-	-	646	14	646	14	2
U.S. Treasury securities and							

obligations of U.S. government corporations and agencies	-	-	-	-	-	-	-
	$ 333	$ 4	$ 3,054	$ 55	$ 3,387	$ 59	11

60

NOTE 4 – INVESTMENT SECURITIES – CONTINUED

According to the most recent accounting guidance, for securities in an unrealized loss position, the Company is required to assess whether the Company has the intent to sell the security or more likely than not will be required to sell the security before the anticipated recovery. If either of these conditions is met, the Company is required to recognize an other-than-temporary impairment with the entire unrealized loss reported in earnings. For securities in an unrealized loss position that do not meet these conditions, the Company assesses whether the impairment of a security is other-than-temporary. If the impairment is determined to be other-than-temporary, the Company is required to separate the other-than-temporary impairments into two components: the amount representing the credit loss and the amount related to all other factors. The credit loss is the portion of the amortized book value in excess of the net present value of the projected future cash flows discounted at the effective interest rate implicit in the debt security prior to impairment. The credit loss component of other-than-temporary impairments is reported in earnings, whereas the amount relating to factors other than credit losses are recorded in other comprehensive income, net of taxes.

Management has evaluated each security in a significant unrealized loss position. For the year ended December 31, 2009, the Company realized $443,000 in other than temporary impairments. The single largest accumulated loss was in the equity portfolio and totaled $337,000. The second largest loss position was in the bond portfolio and totaled $332,000. The third largest loss position was in the equity portfolio and totaled $163,000. Most unrealized losses in the fixed income portfolio are interest rate driven as opposed to credit quality driven and management believes no ultimate loss will be realized. The Company has no material exposure to sub-prime mortgage loans and less than 2% of the fixed income investment portfolio is rated below investment grade. In evaluating whether or not the equity loss positions were other-than-temporary impairments, Management evaluated financial information on each company and reviewed analyst reports from at least two independent sources. Based on a review of the available financial information, the prospect for future earnings of each company and consideration of the Company's intent and ability to hold the securities until market values recovered, it was determined that the remaining securities in an accumulated loss position in the portfolio were temporary impairments.

NOTE 5 – NET INVESTMENT INCOME

Major categories of investment income are summarized as follows:

	(Dollars in thousands)	
	Year ended December 31,	
	2009	2008
Fixed maturities	$ 4,075	$ 4,357
Equity securities	199	364
Mortgage loans on real estate	62	32
Investment real estate	82	65
Policy loans	73	68
Company owned life insurance	740	(543)
Other, principally short-term investments	346	367
	5,577	4,710
	288	342

Less: Investment expenses				
Net investment income	$	5,289	$	4,368

An analysis of investment gains (losses) follows:	Year ended December 31,			
		2009		2008
Net realized investment gains (losses):				
Fixed maturities	$	548	$	179
Equity securities		234		1,313
Other, principally real estate		18		432
Other than temporary impairments		(443)		(2,973)
	$	357	$	(1,049)

61

NOTE 5 – NET INVESTMENT INCOME – CONTINUED

An analysis of the net change in unrealized appreciation on available-for-sale securities follows:

	(Dollars in thousands) Year ended December 31,	
	2009	2008
Net change in unrealized appreciation on available-for-sale securities before deferred tax	$ 5,304	$ (8,335)
Deferred income tax	(1,784)	2,188
Net change in unrealized appreciation on available-for-sale securities	$ 3,520	$ (6,147)

NOTE 6 – FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Our securities available-for-sale consists of fixed maturity and equity securities which are recorded at fair value in the accompanying consolidated balance sheets. The change in the fair value of these investments, unless deemed to be other than temporarily impaired, is recorded as a component of other comprehensive income.

We are permitted to elect to measure financial instruments and certain other items at fair value, with the change in fair value recorded in earnings. We elected not to measure any eligible items using the fair value option.

Accounting standards define fair value as the price that would be received to sell an asset or would be paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establishes a framework to make the measurement of fair value more consistent and comparable. In determining fair value, we primarily use prices and other relevant information generated by market transactions involving identical or comparable assets.

The Company categorizes assets and liabilities carried at their fair value based upon a fair value hierarchy:

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

Level 1 assets and liabilities consist of money market fund deposits and certain of our marketable debt and equity instruments, including equity instruments offsetting deferred compensation, that are traded in an active market with sufficient volume and frequency of transactions.

Level 2 - Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets with insufficient volume or infrequent transactions (less active markets); or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 2 assets include certain of our marketable debt and equity instruments with quoted market prices that are traded in less active markets or priced using a quoted market price for similar instruments. Level 2 assets also include marketable equity instruments with security-specific restrictions that would transfer to the buyer, marketable debt instruments priced using indicator prices which represent non-binding market consensus prices that can be corroborated by observable market quotes, as well as derivative contracts and debt instruments priced using inputs that are observable in the market or can be derived principally from or corroborated by observable market data. Marketable debt instruments in this category generally include commercial paper, bank time deposits, repurchase agreements for fixed-income instruments, and a majority of floating-rate notes, corporate bonds, and municipal bonds.

Level 3 - Unobservable inputs to the valuation methodology that are significant to the measurement of fair value of assets or liabilities.

NOTE 6 – FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES – CONTINUED

Level 3 assets and liabilities include marketable debt instruments, non-marketable equity investments, derivative contracts, and company issued debt whose values are determined using inputs that are both unobservable and significant to the values of the instruments being measured. Level 3 assets also include marketable debt instruments that are priced using indicator prices that we were unable to corroborate with observable market quotes.

Marketable debt instruments in this category generally include asset-backed securities and certain of our floating-rate notes, corporate bonds, and municipal bonds.

Assets/Liabilities Measured at Fair Value on a Recurring Basis
Financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2009 are summarized in the following table by the type of inputs applicable to the fair value measurements (in thousands):

	Fair Value Measurements at Reporting Date Using			
Description	Total	Level 1	Level 2	Level 3
Financial Assets				
Fixed maturities available-for-sale	$ 70,269	$ 9,214	$ 60,478	$ 577
Short-term investments	-	-	-	-
Trading securities	374	374	-	-
Equity securities available-for-sale	9,035	8,373	-	662
Total Financial Assets	$ 79,678	$ 17,961	$ 60,478	$ 1,239
Financial Liabilities				
Interest rate swap	$ 60	$ -	$ -	$ 60
Total Financial Liabilities	$ 60	$ -	$ -	$ 60

The table below presents reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2009:

	For the year ended December 31, 2009		
(In Thousands)	Fixed Maturities Available for sale	Equity Securities Available for Sale	Interest Rate Swap
Beginning balance	$ 652	$ 733	$ (316)

Total gains or losses (realized and unrealized):			
Included in earnings	-	-	-
Included in other comprehensive income	(75)	(71)	256
Purchases, sales, issuances and settlements, net	-	-	-
Transfers in/(out) of Level 3	-	-	-
Ending balance	$ 577	$ 662	$ (60)
The amount of total gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets and liabilities still held as of December 31, 2009	$ -	$ -	$ -

For the year ended December 31, 2009, there were no assets or liabilities measured at fair values on a nonrecurring basis.

63

NOTE 6 – FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES – CONTINUED

The table below presents reconciliation for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31, 2008:

	For the year ended December 31, 2008		
	Fixed Maturities Available for sale	Equity Securities Available for Sale	Interest Rate Swap
(In Thousands)			
Year ended December 31, 2008			
Beginning balance	$ 702	$ 999	$ (88)
Total gains or losses (realized and unrealized):			
Included in earnings	-	-	-
Included in other comprehensive income	(50)	(266)	(228)
Purchases, sales, issuances and settlements, net	-	-	-
Transfers in/(out) of Level 3	-	-	-
Ending balance	$ 652	$ 733	$ (316)
The amount of total gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets and liabilities still held as of December 31, 2008	$ -	$ -	$ -

For the year ended December 31, 2008, there were no assets or liabilities measured at fair values on a nonrecurring basis.

The Company is exposed to certain risks in the normal course of its business operations. The primary risk that is managed through the use of derivatives is interest rate risk on floating rate borrowings. This risk is managed through the use of interest rate swaps which are designated as cash flow hedges. For cash flow hedges, the effective portion of the gain or loss on the interest rate swap is included as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged transaction is recognized in earnings. The Company does not hold or issue derivatives that are not designated as hedging instruments. Please see Note 9 for additional information about the interest rate swaps.

The following methods and assumptions were used to estimate fair value of each class of financial instrument for which it is practical to estimate that value:

Cash and cash equivalents—the carrying amount is a reasonable estimate of fair value.

Mortgage receivables—the carrying amount is a reasonable estimate of fair value to the restrictive nature and limited marketability of the mortgage notes.

Other invested assets—the carrying amount is a reasonable estimate of fair value.

Other policyholder funds—the carrying amount is a reasonable estimate of fair value.

Debt—the carrying amount is a reasonable estimate of fair value.

The carrying amount and estimate fair value of the Company's financial instruments as of December 31, are as follows:

	In Thousands of Dollars at December 31,			
	2009		2008	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Assets and related instruments				
Mortgage loans	$ 1,041	$ 1,041	$ 502	$ 502
Policy loans	1,018	1,018	968	968
Company owned life insurance	5,197	5,197	1,957	1,957
Other invested assets	3,933	3,933	4,557	4,557
Liabilities and related instruments				
Other policyholder funds	1,347	1,347	1,344	1,344
Long-term debt	12,372	12,372	12,372	12,372

NOTE 7 - PROPERTY AND EQUIPMENT

At December 31, property and equipment consisted of the following:

	(Dollars in Thousands)	
	2009	2008
Building and improvements	$ 3,196	$ 3,196
Electronic data processing equipment	2,472	2,549
Furniture and fixtures	1,005	1,085
	6,673	6,830
Less accumulated depreciation	4,136	3,986
	$ 2,537	$ 2,844

Depreciation expense for the year ended December 31, 2009 was $424,000 ($454,000 for the year ended December 31, 2008).

NOTE 8 – INCOME TAXES

The Company recognizes tax-related interest and penalties as a component of tax expense. The Company incurred $-0- in interest and penalties as of both December 31, 2009 and December 31, 2008. The Company files income tax returns in the U.S. federal jurisdiction and various states. The Company is not subject to examinations by authorities related to its U.S. federal or state income tax filings for years prior to 2006. The Internal Revenue Service completed an examination during 2008 of the Company's 2005 Federal Income Tax Return. No material adjustments were made as a result of this examination. No income tax returns are currently under examination by the Internal Revenue Service or any state or local taxing authority. Tax returns have been filed through the year 2008.

Net deferred tax liabilities are determined based on the estimated future tax effects of differences between the financial statement and tax basis of assets and liabilities given the provisions of the enacted tax laws. Management believes that, based on its historical pattern of taxable income, the Company will produce sufficient income in the future to realize its deferred tax assets. The Company recognized a net deferred tax liability position of $61,000 in 2009 and net deferred tax asset position of $1,839,000 in 2008.

NOTE 8 – INCOME TAXES

The tax effect of significant differences representing deferred tax assets and liabilities are as follows:

	(Dollars in Thousands)	
	December 31, 2009	December 31, 2008
General insurance expenses	$ 1,135	$ 769
Unearned premiums	1,814	1,885
Claims liabilities	298	337
Unrealized losses on securities available-for-sale	-	392
Other than temporary impairments on securities owned	501	734
Deferred tax assets	3,748	4,117
Depreciation	(126)	(118)
Deferred policy acquisition costs	(2,291)	(2,160)
Unrealized gains on securities available-for-sale	(1,392)	-
Deferred tax liabilities	(3,809)	(2,278)
Net deferred tax (liability) asset	$ (61)	$ 1,839

Total income tax expense varies from amounts computed by applying current federal income tax rates to income before income taxes. The reason for these differences and the approximate tax effects are as follows:

	(Dollars in thousands)	
	Year ended December 31,	
	2009	2008
Federal income tax rate applied to pre-tax income	$ 1,862	$ (2,657)

Dividends received deduction and tax-exempt interest	(201)	(137)
Company owned life insurance	(252)	185
Small life deduction	(145)	(174)
Other, net	(12)	173
Federal income tax expense (benefit)	$ 1,252	$ (2,610)

The appropriate income tax effects of changes in temporary differences are as follows:

	Year ended December 31,	
	2009	2008
Deferred policy acquisition costs	$ 131	$ (261)
Other-than-temporary impairments	233	734
Unearned premiums	71	362
General insurance expenses	(366)	(69)
Depreciation	8	40
Claim liabilities	39	79
	$ 116	$ 885

NOTE 8 – INCOME TAXES – CONTINUED

Under pre-1984 life insurance company tax laws, a portion of NSIC's gain from operations was not subject to current income taxation, but was accumulated for tax purposes in a memorandum account designated "policyholders' surplus". The aggregate balance in this account, $2,520,000 at December 31, 2009, would be taxed at current rates only if distributed to shareholders or if the account exceeded a prescribed minimum. The Deficit Reduction Act of 1984 eliminated additions to policyholders' surplus for 1984 and thereafter. Deferred taxes have not been provided on amounts designated as policyholders' surplus. The deferred income tax liability not recognized is approximately $857,000 at December 31, 2009

NOTE 9 – NOTES PAYABLE AND LONG-TERM DEBT

Long-term debt consisted of the following as of December 31, 2009 and December 31, 2008:

	(Dollars in thousands)	
	2009	2008
Subordinated debentures issued on December 15, 2005 with fixed interest rate of 8.83% each distribution period thereafter until December 15, 2015 when the coupon rate shall equal the 3-month LIBOR plus 3.75% applied to the outstanding principal; maturity December 2035. Interest payments due quarterly. All may be redeemed at any time following the tenth anniversary of issuance. Unsecured.	$ 9,279	$ 9,279
Subordinated debentures issued on June 21, 2007 with a floating interest rate equal to the 3 Month LIBOR plus 3.40% applied to the outstanding principal; maturity June 15, 2037. Interest payments due quarterly. All may be	3,093	3,093

redeemed at any time following the fifth anniversary of issuance. Unsecured.		
	$ 12,372	$ 12,372

The $9,279,000 of subordinated debentures is due in 2035 and $3,093,000 of subordinated debentures is due in 2037.

The subordinated debentures (debentures) have the same maturities and other applicable terms and features as the associated trust preferred securities (TPS). Payment of interest may be deferred for up to 20 consecutive quarters; however, stockholder dividends cannot be paid during any extended interest payment period or any time the debentures are in default. All have stated maturities of thirty years. None of the securities require the Company to maintain minimum financial covenants. The Company has guaranteed that amounts paid to the Trusts (discussed in Note 2) will be remitted to the holders of the associated TPS. This guarantee, when taken together with the obligations of the Company under the debentures, the Indentures pursuant to which the debentures were issued, and the related trust agreement (including obligations to pay related trust fees, expenses, debt and other obligations with respect to the TPS), provides a full and unconditional guarantee of amounts due the Trusts. The amount guaranteed is not expected to at any time exceed the obligations of the TPS, and no additional liability has been recorded related to the guarantee.

NOTE 9 – NOTES PAYABLE AND LONG-TERM DEBT – CONTINUED

unconditional guarantee of amounts due the Trusts. The amount guaranteed is not expected to at any time exceed the obligations of the TPS, and no additional liability has been recorded related to the guarantee.

On September 13, 2007, the Company entered into a 5 year swap effective September 17, 2007 with a notional amount of $3,000,000 and designated the swap as a hedge against changes in cash flows attributable to changes in the benchmark interest rate (LIBOR) associated with the subordinated debentures issued on June 21, 2007. Commencing December 17, 2007, under the terms of the swap, the Company will pay interest at the three-month LIBOR rate plus 3.4% and receive interest at the fixed rate of 8.34%.

On March 19, 2009, the Company entered into a forward swap effective September 17, 2012, which will also hedge against changes in cash flows following the termination of the 5 year swap agreement discussed previously. Commencing September 17, 2012, under the terms of the forward swap, the Company will pay interest at the three-month LIBOR rate plus 3.4% and receive interest at the fixed rate of 7.02%. This forward swap will effectively fix the interest rate on $3,000,000 in debt until September of 2019.

The swaps entered into in 2007 and 2009 have fair values of $245,000 (liability) and $185,000 (asset), respectively, for a net liability of $60,000 at December 31, 2009 ($316,000 at December 31, 2008) which is reported as a component of other liabilities on the consolidated balance sheets. A net valuation gain of $256,000 is included in accumulated other comprehensive income related to the swap agreements for the current period. A net valuation loss of $228,000 was included in accumulated other comprehensive income related to the swap in the prior year.

We use dollar offset at the hedge's inception and for each reporting period thereafter to assess whether the derivative used in a hedging transaction is expected to be, and has been, effective in offsetting changes in the fair value of the hedged item. Since inception no portion of the hedged item has been deemed ineffective. For all hedges, we discontinue hedge accounting if it is determined that a derivative is not expected to be, or has ceased to be, effective as a hedge.

The Company's interest rate swaps include provisions requiring the Company to post collateral when the derivative is in a net liability position. The Company has posted collateral of $469,000. Please see Note 6 for additional information about the interest rate swaps.

In December of 2009, the Company obtained an unsecured line of credit for $700,000, with an interest rate of 5%, to be made available for general corporate purposes. The line of credit matures December 25, 2010. No funds were drawn on this line at December 31, 2009.

NOTE 10 – POLICY AND CLAIM RESERVES

The Company regularly updates its reserve estimates as new information becomes available and events occur that may impact the resolution of unsettled claims. Changes in prior years' reserve estimates are reflected in the results of operations in the year such changes are determined. The following table is a reconciliation of beginning and ending property and casualty reserve balances for claims and claim adjustment expense for the years ended December 31:

	(Dollars in thousands)	
	2009	2008
Claims and claim adjustment expense		

reserves at beginning of year	$ 14,436	$ 11,973
Less reinsurance recoverables on		
unpaid losses	2,421	555
Net balances at beginning of year	12,015	11,418
Provision for claims and claim adjustment		
expenses for claims arising in current year	34,239	43,284
Estimated claims and claim adjustment		
expenses for claims arising in prior years	(2,626)	(2,374)
Total increases	31,613	40,910
Claims and claim adjustment expense		
payments for claims arising in:		
Current year	25,941	35,516
Prior years	5,590	4,797
Total payments	31,531	40,313
Net balance at end of year	12,097	12,015
Plus reinsurance recoverables on		
unpaid losses	549	2,421
Claims and claim adjustment expense		
reserves at end of year	$ 12,646	$ 14,436

The 2009 decline in the provision for claims and claim adjustment expenses arising from claims in the current year and the ending reinsurance recoverable on unpaid losses are attributable to the absence of hurricane losses during the year. The decrease in provision for claims and claim adjustment expenses for prior years (net of reinsurance recoveries) for 2008 is primarily due to reductions in incurred but not reported loss reserves on dwelling property lines of business.

NOTE 10 – POLICY AND CLAIM RESERVES – CONTINUED

The Company has a geographic exposure to catastrophe losses in certain areas of the country. Catastrophes can be caused by various events including hurricanes, windstorms, earthquakes, hail, severe winter weather, explosions and fires, and the incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophe losses are restricted to small geographic areas; however, hurricanes and earthquakes may produce significant damage in large, heavily populated areas. The Company generally seeks to reduce its exposure to catastrophes through individual risk selection and the purchase of catastrophe reinsurance. At December 31, 2009, the Company's estimate of unpaid losses and adjustment expenses for hurricane related claims incurred in prior years totaled $787,000 before reinsurance ($758,000 in 2008). Because the Company has exhausted its catastrophe coverage limits available for Hurricane Katrina any additional development will not be covered by reinsurance. The Company maintains case reserves of $519,000 for losses in excess of catastrophe reinsurance ($594,000 in 2008).

NOTE 11 – REINSURANCE

The Company's insurance operations participate in reinsurance in order to limit losses, minimize exposure to large risks, provide additional capacity for future growth and effect business-sharing arrangements. Life reinsurance is accomplished through yearly renewable term. Property and casualty reinsurance is placed on both a quota-share and excess of loss basis. Reinsurance ceded arrangements do not discharge the insurance subsidiaries as the primary insurer, except for cases involving a novation. Failure of reinsurers to honor their obligations could result in losses to the insurance subsidiaries. The insurance subsidiaries evaluate the financial conditions of their reinsurers and monitor concentrations of credit risk arising from similar geographic regions, activities, or economic characteristics of the reinsurers to minimize their exposure to significant losses from reinsurance insolvencies.

At December 31, 2009, the largest reinsurance recoverable of a single reinsurer was $95,000 ($607,000 in 2008). The amounts of recoveries pertaining to reinsurance contracts that were deducted from losses incurred during 2009 and 2008 were approximately $-0- and $12,582,000, respectively. The Company incurred no losses from covered events occurring in 2009. Amounts reported as ceded incurred losses in 2009 were related to development of losses from prior year catastrophes.

The effect of reinsurance on premiums written and earned was as follows:

	(Dollars in Thousands)			
	2009			
	Life		Property & Casualty	
	Written	Earned	Written	Earned
Direct	$ 7,251	$ 7,247	$ 58,185	$ 59,213
Assumed	-	-	-	-
Ceded	(48)	(48)	(6,660)	(6,818)
Net	$ 7,203	$ 7,199	$ 51,525	$ 52,395

	2008							
	Life				Property & Casualty			
		Written		Earned		Written		Earned
Direct	$	7,049	$	7,003	$	61,197	$	55,866
Assumed		-		-		-		-
Ceded		(47)		(47)		(6,487)		(6,558)
Net	$	7,002	$	6,956	$	54,710	$	49,308

69

NOTE 12 – EMPLOYEE BENEFIT PLANS

In 1989, the Company and its subsidiaries established a retirement savings plan (401K Plan) and transferred the assets from the defined contribution profit sharing plan into the new plan. All full-time employees who have completed six months of service at the beginning of any calendar quarter are eligible to participate and all employee contributions are fully vested for employees who have completed 1,000 hours of service in the year of contribution. Company matching contributions for 2009 and 2008 amounted to $219,000 and $255,000, respectively. The Company contributes dollar-for-dollar matching contributions up to 5% of compensation subject to government limitations.

In 1987, the Company established a non-qualified deferred compensation plan for its Board of Directors. The Board members had an option of deferring their fees to a cash account or to a stock account and all share deferrals are recorded at the fair market value on the date of the award. The directors' non-qualified deferred compensation plan was frozen on December 31, 2004, and deferrals are no longer allowed. A new non-qualified plan became effective January 1, 2006 under which directors are allowed to defer all or a portion of directors' fees into various investment options. The supplemental executive retirement plan (SERP) became effective March 1, 2008 and covers named executive officers with the Company contributing 15% of executive compensation to the plan. Contributions to the plan are fully vested upon the earlier of death, disability, change in control, or ten years of participation in the plan. Costs for amounts credited of the non-qualified deferred compensation plans for 2009 and 2008 amounted to approximately 388,000 and ($349,000), respectively.

NOTE 13 – REGULATORY REQUIREMENTS AND DIVIDEND RESTRICTIONS

The amount of dividends paid from NSIC to the Company in any year may not exceed, without prior approval of regulatory authorities, the greater of 10% of statutory surplus as of the end of the preceding year, or the statutory net gain from operations for the preceding year. At December 31, 2009, NSIC's retained earnings unrestricted for the payment of dividends in 2010 amounted to $1,250,000.

NSFC is similarly restricted in the amount of dividends payable to the Company; dividends may not exceed the greater of 10% of statutory surplus as of the end of the preceding year, or net income for the preceding year. At December 31, 2009, NSFC's retained earnings unrestricted for the payment of dividends in 2010 amounted to $4,179,000.

At December 31, 2009, securities with market values of $3,530,000 ($3,812,000 at December 31, 2008) were deposited with various states pursuant to statutory requirements.

Under applicable Alabama insurance laws and regulations, NSFC is required to maintain a minimum total surplus (to include both paid-in and contributed and unassigned surplus) of $100,000.

Under applicable Alabama insurance laws and regulations, NSIC is required to maintain a minimum total surplus (to include both paid-in and contributed and unassigned surplus) of $200,000.

Under applicable Alabama insurance laws and regulations, Omega is required to maintain a minimum total surplus (to include both paid-in and contributed and unassigned surplus) of $500,000.

NOTE 14 – SHAREHOLDERS' EQUITY

Preferred Stock

The Preferred Stock may be issued in one or more series as shall from time to time be determined and authorized by the Board of Directors. The directors may make specific provisions regarding (a) the voting rights, if any (b) whether such dividends are to be cumulative or noncumulative (c) the redemption provisions, if any (d) participating rights, if any (e) any sinking fund or other retirement provisions (f) dividend rates (g) the number of shares of such series and (h) liquidation preference.

Common Stock

The holders of the Class A Common Stock will have one-twentieth of one vote per share, and the holders of the common stock will have one vote per share.

In the event of any liquidation, dissolution or distribution of the assets of the Company remaining after the payments to the holders of the Preferred Stock of the full preferential amounts to which they may be entitled as provided in the resolution or resolutions creating any series thereof, the remaining assets of the Company shall be divided and distributed among the holders of both classes of common stock, except as may otherwise be provided in any such resolution or resolutions.

An amendment changing the number of authorized shares of common stock from 10,000,000 to 3,000,000 was approved by the shareholders at the 2009 Annual Meeting on May 14, 2009.

NOTE 15 – INDUSTRY SEGMENTS

The Company and its subsidiaries operate primarily in the insurance industry. Selected balance sheet information by industry segment for the years ended December 31, 2009 and 2008 is summarized below:

(Dollars in thousands)		Total		P&C Insurance Operations		Life Insurance Operations		Non-Insurance Operations
December 31, 2009								
Selected Assets								
Investments	$	101,720	$	60,768	$	40,079	$	873
Reinsurance recoverable	$	784	$	784	$	-	$	-
Deferred policy acquisition costs	$	10,210	$	3,915	$	6,295	$	-
Total Assets	$	131,396	$	79,321	$	49,872	$	2,203
Total Liabilities	$	90,228	$	43,099	$	34,348	$	12,781

(Dollars in thousands)		Total		P&C Insurance Operations		Life Insurance Operations		Non-Insurance Operations
December 31, 2008								
Selected Assets								
Investments	$	90,132	$	56,422	$	33,200	$	510
Reinsurance recoverable	$	4,146	$	4,146	$	-	$	-
Deferred policy acquisition costs	$	9,825	$	4,037	$	5,788	$	-
Total Assets	$	124,890	$	78,802	$	43,653	$	2,435

Total Liabilities	$	90,242	$	45,476	$	31,627	$	13,139

71

NOTE 15 – INDUSTRY SEGMENTS – CONTINUED

Premium revenues and operating income by industry segment for the years ended December 31, 2009 and 2008 are summarized below:

(Dollars in thousands)	Total	P&C Insurance Operations	Life Insurance Operations	Non-Insurance Operations
Year ended December 31, 2009				
REVENUE				
Net premiums earned	$ 59,594	$ 52,395	$ 7,199	$ -
Net investment income	5,289	3,125	2,114	50
Net realized investment gains	357	120	234	3
Other income	764	761	3	-
	66,004	56,401	9,550	53
BENEFITS AND EXPENSES				
Policyholder benefits paid or provided	35,839	30,908	4,931	-
Amortization of deferred policy acquisition costs	3,673	3,397	276	-
Commissions	7,863	7,317	546	-
General and administrative expenses	10,396	6,775	2,543	1,078
Insurance taxes, licenses and fees	1,631	1,387	244	-
Interest expense	1,126	-	49	1,077
	60,528	49,784	8,589	2,155
Income (Loss) Before Income Taxes	5,476	6,617	961	(2,102)
INCOME TAX EXPENSE (BENEFIT)				
Current	1,136	1,369	105	(338)

Deferred	116	97	392	(373)
	1,252	1,466	497	(711)
NET INCOME (LOSS)	$ 4,224	$ 5,151	$ 464	$ (1,391)

72

NOTE 15 – INDUSTRY SEGMENTS – CONTINUED

(Dollars in thousands)

	Total	P&C Insurance Operations	Life Insurance Operations	Non-Insurance Operations
Year ended December 31, 2008				
REVENUE				
Net premiums earned	$ 56,264	$ 49,308	$ 6,956	$ -
Net investment income	4,368	2,309	1,940	119
Net realized investment (losses) gains	(1,049)	372	(1,423)	2
Other income	1,107	1,047	60	-
	60,690	53,036	7,533	121
BENEFITS AND EXPENSES				
Policyholder benefits paid or provided	44,746	39,719	5,027	-
Amortization of deferred policy acquisition costs	4,344	3,312	1,032	-
Commissions	8,262	7,772	490	-
General and administrative expenses	8,558	6,722	1,614	222
Insurance taxes, licenses and fees	1,447	1,159	288	-
Interest expense	1,147	1	61	1,085
	68,504	58,685	8,512	1,307
Loss Before Income Taxes	(7,814)	(5,649)	(979)	(1,186)
INCOME TAX EXPENSE (BENEFIT)				
Current	(3,495)	(2,919)	(281)	(295)
Deferred	885	867	161	(143)
	(2,610)	(2,052)	(120)	(438)

NET LOSS	$	(5,204	)	$	(3,597	)	$	(859	)	$	(748	)

NOTE 16 – CONTINGENCIES

Litigation

The Company and its subsidiaries continue to be named as parties to litigation related to the conduct of their insurance operations. These suits involve alleged breaches of contracts, torts, including bad faith and fraud claims based on alleged wrongful or fraudulent acts of agents of the Company's subsidiaries, and miscellaneous other causes of action. Most of these lawsuits include claims for punitive damages in addition to other specified relief.

The Company's property & casualty subsidiaries are defending a number of matters filed in the aftermath of Hurricanes Katrina and Rita in Mississippi, Louisiana and Alabama. These actions include individual lawsuits and purported statewide class action lawsuits, although to date no class has been certified in any action. These actions make a number of allegations of underpayment of hurricane-related claims, including allegations that the flood exclusion found in the Company's subsidiaries' policies, and in certain actions other insurance companies' policies, is either ambiguous, unenforceable as unconscionable or contrary to public policy, or inapplicable to the damage sustained. The various suits seek a variety of remedies, including actual and/or punitive damages in unspecified amounts and/or declaratory relief. All of these matters are in various stages of development and the Company's subsidiaries intend to vigorously defend them. The outcome of these disputes is currently uncertain.

In 2007, the Company sold substantially all of its interest in a consolidated subsidiary, Mobile Attic, Inc. On July 9, 2009, the Company moved to intervene in a complaint filed by the purchaser of Mobile Attic against the founder and former president/CEO of Mobile Attic and others, regarding the plaintiff's purchase of shares of Mobile Attic. The Company filed a proposed complaint in intervention requesting the Court to find that the Company is not liable for indemnity under the Stock Purchase Agreement, or in the alternative, to award damages to the Company for any loss suffered as a result of the fraudulent actions of the former president/CEO of Mobile Attic and as a result of the negligence of Mobile Attic and its

NOTE 16 – CONTINGENCIES – CONTINUED

auditors in the preparation of Mobile Attic's financial statements. The Court has subsequently granted the Company's motion to intervene and the action is in the initial stages of discovery. No amount has been accrued in these financial statements since the outcome of this matter is uncertain and the amount of liability, if any, cannot be determined.

The Company establishes and maintains reserves on contingent liabilities. In many instances, however, it is not feasible to predict the ultimate outcome with any degree of accuracy. While a resolution of these matters may significantly impact consolidated earnings and the Company's consolidated financial position, it remains management's opinion, based on information presently available, that the ultimate resolution of these matters will not have a material impact on the Company's consolidated financial position.

NOTE 17 –SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest during 2009 was $1,077,000 ($1,085,000 in 2008). Cash received from income taxes in 2009 was $796,000 compared to cash paid for income taxes in 2008 was $500,000.

NOTE 18 – SUBSEQUENT EVENTS

There were no subsequent events requiring adjustment to the condensed consolidated financial statements.

THE NATIONAL SECURITY GROUP, INC.
SCHEDULE I. SUMMARY OF INVESTMENTS (CONSOLIDATED)
(Dollars in Thousands)

	December 31, 2009			December 31, 2008		
	Cost	Fair Value	Amount per the Balance Sheet	Cost	Fair Value	Amount per the Balance Sheet
Securities Held-to-Maturity:						
United States government	$ 441	$ 455	$ 441	$ 4,387	$ 4,435	$ 4,387
States, municipalities and political subdivisions . . .	2,139	2,182	2,139	2,141	2,161	2,141
Mortgage backed securities	3,175	3,251	3,175	4,087	4,066	4,087
Private label mortgage backed securities	187	192	187	249	248	249
Industrial and Miscellaneous	-	-	-	88	85	88
Total Securities Held-to-Maturity	5,942	6,080	5,942	10,952	10,995	10,952
Securities Available-for-Sale:						
Equity Securities:						
Banks and insurance companies	1,489	989	989	1,256	1,699	1,699
Industrial and all other	4,362	8,046	8,046	4,211	5,870	5,870
Total equity securities	5,851	9,035	9,035	5,467	7,569	7,569

. . . .						
Debt Securities:						
United States government	9,532	9,713	9,713	9,551	9,983	9,983
States, municipalities and political subdivisions . . .	15,641	15,516	15,516	13,401	12,607	12,607
Mortgage backed securities	8,203	8,320	8,320	11,101	11,334	11,334
Private label mortgage backed securities	9,634	8,896	8,896	6,590	5,223	5,223
Public Utilities	-	-	-	549	554	554
Industrial and Miscellaneous	26,786	27,824	27,824	20,604	18,406	18,406
Total Debt Securities	69,796	70,269	70,269	61,796	58,107	58,107
Total Available-for-Sale	75,647	79,304	79,304	67,263	65,676	65,676
Total Securities	81,589	85,384	$ 85,246	78,215	76,671	76,628
Trading securities.	314	374	374	354	253	253
Receivable for securities.	96	96	96	513	513	513
Mortgage loans on real estate	1,041	1,041	1,041	502	502	502
Investment real estate	4,815	4,815	4,815	4,754	4,754	4,754
Policy loans	1,018	1,018	1,018	968	968	968
Company owned life insurance.	5,000	5,197	5,197	2,500	1,957	1,957
Other invested assets.	3,933	3,933	3,933	4,557	4,557	4,557

.						
Total investments . . .	$ 97,806	$ 101,858	$ 101,720	$ 92,363	$ 90,175	$ 90,132

THE NATIONAL SECURITY GROUP, INC.
(PARENT COMPANY)
SCHEDULE II - CONDENSED FINANCIAL INFORMATION OF REGISTRANT
BALANCE SHEETS
(Amounts in thousands)

	December 31,	
	2009	2008
Assets		
Cash	$ 382	$ 454
Investment in subsidiaries (equity method) eliminated upon consolidation	51,658	45,380
Other assets	2,866	2,269
Total Assets	$ 54,906	$ 48,103
Liabilities and Shareholders' Equity		
Accrued general expenses	$ 1,366	$ 1,083
Notes payable	12,372	12,372
Total Liabilities	13,738	13,455
Total Shareholders' Equity	41,168	34,648
Total Liabilities and Shareholders' Equity	$ 54,906	$ 48,103

THE NATIONAL SECURITY GROUP, INC. (PARENT COMPANY)
SCHEDULE II - CONDENSED FINANCIAL INFORMATION OF REGISTRANT
STATEMENTS OF INCOME (LOSS)
(Amounts in thousands)

	Years Ended December 31,	
	2009	2008
Income		
Dividends (eliminated upon consolidation)	$ 2,800	$ -
Other income	52	119
	2,852	119
Expenses		
State taxes	1	1
Other expenses	2,154	1,300
	2,155	1,301
Income before income taxes and equity in undistributed earnings (loss) of subsidiaries	697	(1,182)
Income tax (benefit) expense	(711)	(437)
Income (loss) before equity in undistributed earnings (loss) of subsidiaries	1,408	(745)
Equity in undistributed (losses) earnings of subsidiaries	2,816	(4,459)
Net (loss) income	$ 4,224	$ (5,204)

THE NATIONAL SECURITY GROUP, INC. (PARENT COMPANY)
SCHEDULE II - CONDENSED FINANCIAL INFORMATION OF REGISTRANT
STATEMENTS OF CASH FLOWS
(Amounts in thousands)

	Years Ended December 31, 2009	2008
Cash flows from operating activities:		
Net income (loss)	$ 4,224	$ (5,204)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Equity in undistributed loss (income) of subsidiaries	(2,816)	4,459
Change in other assets	(539)	3,246
Change in accrued general expenses	539	(659)
Net cash provided by operating activities	1,408	1,842
Cash flows from investing activities:		
Net cash provided by investing activities	-	-
Net cash provided by investing activities	-	-
Cash flows from financing activities:		
Cash dividends	(1,480)	(2,220)
Net cash used in financing activities	(1,480)	(2,220)
Net (decrease) increase in cash and cash equivalents	(72)	(378)
Cash at beginning of year	454	832

Cash at end of year	$	382	$	454

78

THE NATIONAL SECURITY GROUP, INC. (PARENT COMPANY)
Notes to Condensed Financial Information of Registrant

Note 1-Basis of Presentation

Pursuant to the rules and regulations of the Securities and Exchange Commission, the Condensed Financial Information of the Registrant does not include all of the information and notes normally included with financial statements prepared in accordance with generally accepted accounting principles. It is, therefore, suggested that this Condensed Financial Information be read in conjunction with the Consolidated Financial Statements and Notes thereto included in the Registrant's Annual Report as referenced in Form 10-K, Part II, Item 8, page 44.

Note 2-Cash Dividends from Subsidiaries

In 2009, dividends of $2.8 million were paid to the Registrant by its subsidiaries. No dividends were received from subsidiaries during 2008.

THE NATIONAL SECURITY GROUP, INC.
SCHEDULE III SUPPLEMENTARY INSURANCE INFORMATION (CONSOLIDATED)
(Amounts in thousands)

	Deferred Acquisition Costs	Future Policy Benefits	Unearned Premiums
At December 31, 2009:			
Life and accident and health insurance	$ 6,295	$ 30,726	$ 16
Property and casualty insurance	3,915	-	27,365
Total	$ 10,210	$ 30,726	$ 27,381
At December 31, 2008:			
Life and accident and health insurance	$ 5,788	$ 29,770	$ 44
Property and casualty insurance	4,037	-	27,720
Total	$ 9,825	$ 29,770	$ 27,764

	Premium Revenue	Net Investment Income	Other Income	Benefits, Claims, Losses and Settlement Expenses	Commissions, Amortization of Deferred Policy Acquisition Costs	General Expenses, Taxes, Licenses and Fees
For the year ended December 31, 2009:						
Life and accident and health insurance	$ 7,199	$ 2,114	$ 3	$ 4,931	$ 822	$ 2,787
Property and casualty insurance	52,395	3,125	761	30,908	10,714	8,162
Other	-	50	-	-	-	1,078
Total	$ 59,594	$ 5,289	$ 764	$ 35,839	$ 11,536	$ 12,027
For the year ended December 31, 2008:						
Life and accident and health	$ 6,956	$ 1,940	$ 60	$ 5,027	$ 1,522	$ 1,614

insurance						
Property and casualty insurance	49,308	2,309	1,047	39,719	11,084	6,722
Other	-	119	-	-	-	222
Total	$ 56,264	$ 4,368	$ 1,107	$ 44,746	$ 12,606	$ 10,005

Note: Investment income and other operating expenses are reported separately by segment and not allocated.

80

THE NATIONAL SECURITY GROUP, INC.
SCHEDULE IV. REINSURANCE (CONSOLIDATED)
(Amounts in thousands)

	Gross Amount	Ceded to Other Companies	Assumed from Other Companies	Net Amount	Percentage of Amount Assumed to Net
For the year ended December 31, 2009					
Life insurance in force	$ 215,028	$ 12,034	$ -	$ 202,994	0.00 %
Premiums:					
Life insurance and accident and health insurance	7,247	48	-	7,199	0.00 %
Property and casualty insurance	59,213	6,818	-	52,395	0.00 %
Total premiums	$ 66,460	$ 6,866	$ -	$ 59,594	0.00 %
For the year ended December 31, 2008					
Life insurance in force	$ 214,160	$ 10,115	$ -	$ 204,045	0.00 %
Premiums:					
Life insurance and accident and health insurance	7,003	47	-	6,956	0.00 %
Property and casualty insurance	55,866	6,558	-	49,308	0.00 %

Total premiums	$ 62,869	$ 6,605	$ -	$ 56,264	0.00 %

For the year ended
December 31, 2006

81

The National Security Group, Inc

Schedule V. Valuation and Qualifying Accounts

Years ended December 31, 2009 and 2008

	2009	2008
	(Dollars in thousands)	
Balance, January 1	$ 59	$ 110
Additions	0	0
Deletions	59	51
Balance, December 31	$ 0	$ 59

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

Item 9A. Controls and Procedures

Company management, including the Chief Executive Officer and Chief Financial Officer, have conducted an evaluation of the effectiveness of disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective in ensuring that all material information required to be filed in this annual report has been made known to them in a timely fashion. There have been no significant changes in internal controls, or in factors that could significantly affect internal controls, subsequent to the date the Chief Executive Officer and Chief Financial Officer completed their evaluation.

Management's Report on Internal Control over Financial Reporting

Management of The National Security Group, Inc. is responsible for establishing and maintaining effective internal control over financial reporting. The Company's internal control system was designed to provide reasonable assurance to management and board of directors regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles (GAAP).

The Company's internal control over financial reporting includes those policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, management concluded that the company's internal control over financial reporting was effective as of December 31, 2009.

This annual report does not include an attestation report of the company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the company to provide only management's report in this annual report.

Item 9B. Other Information

None

83

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Executive Officers

JACK E. BRUNSON (52) has served as a director since 1999 and as President of NSFC since 1997. He also serves on the Boards of Directors of NSFC and Omega. He joined the Company in 1982. Mr. Brunson is a Chartered Property and Casualty Underwriter.

W. L. BRUNSON, JR. (51) has served as a director since 1999 and as President and Chief Executive Officer of the Company since 2000. He also holds the position of President of NSIC. He joined the Company in 1983. Mr. Brunson is also a director of NSFC, NATSCO, NSIC, and Omega. Mr. Brunson is a member of the Alabama State Bar.

BRIAN R. MCLEOD (41) currently serves as Vice President of Finance & Operations, CFO and Treasurer of the Company. From 1992-2002 he served as Controller. He joined the Company in 1992. Mr. McLeod is a Director of NSIC, NSFC, Omega and NATSCO. Mr. McLeod is also a member of the Board of Directors for Trinity Bank, a community bank in Dothan, Alabama. Mr. McLeod is a Certified Public Accountant.

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010 with respect to directors of the Company and Corporate Governance, is incorporated herein by reference in response to this item.

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010 with respect to Audit Committee and Audit Committee financial expert, is incorporated herein by reference in response to this item.

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010 with respect to information on the beneficial ownership reporting for directors and executive officers, is incorporated herein by reference in response to this item.

Item 11. Executive Compensation

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010, with respect to executive compensation and transactions, is incorporated herein by reference in response to this item.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010, with respect to security ownership of certain beneficial owners and management is incorporated herein by reference to this item.

Item 13. Certain Relationships and Related Transactions and Director Independence

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010, with respect to certain relationships and related transactions, is incorporated herein by reference in response to this item.

Item 14. Principal Accounting Fees and Services

The information contained in The National Security Group's definitive proxy statement for the 2010 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission on or before April 12, 2010, with respect to principal accountant fees and services, is incorporated herein by reference in response to this item.

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) The following documents are filed as part of this report:

1. Consolidated financial statements, notes thereto and related information of The National Security Group, Inc. (the "Company") are included in Item 8 of Part II of this report:

Report of Independent Registered Public Accounting Firm

Consolidated Statements of Operation – Years ended December 31, 2009 and 2008

Consolidated Balance Sheets – December 31, 2009 and 2008

Consolidated Statements of Shareholders' Equity – Years ended December 31, 2009 and 2008

Consolidated Statements of Cash Flows – Years ended December 31, 2009 and 2008

Consolidated Notes to the Financial Statements

2. Additional financial statement schedules and report of independent registered accounting firm are furnished herewith pursuant to the requirements of Form 10-K:

The National Security Group, Inc.

Schedule I	Summary of Investments Other Than Investments in Related Parties
Schedule II	Condensed Financial Information of Registrant
Schedule III	Supplementary Insurance Information (Consolidated)
Schedule IV	Reinsurance (Consolidated)
Schedule V	Valuation and Qualifying Accounts

3. Exhibits filed as part of this Form 10-K:

11. Computation of Earnings Per Share Filed Herewith, See Note 1 to Consolidated Financial Statements.

14. Code of Ethics, see additional information in Part 1, Item 1 of this report.

21. Subsidiaries of the registrant.

31.1 Certification of Chief Executive Officer Pursuant to 18 U. S. C. Section 1350, as Adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer Pursuant to 18 U. S. C. Section 1350, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32. Certification Chief Executive Officer and Chief Financial Officer Pursuant to 18 U. S. C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) During the last fiscal quarter of the period covered by this Report, the Company filed the following Current Reports on Form 8-K:

Date of Report	Date Filed	Description
November 13, 2009	November 13, 2009	Press release announcing financial results for period ended September 30, 2009.
October 16, 2009	October 19, 2009	Press release announcing quarterly dividend.

SIGNATURE

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

THE NATIONAL SECURITY GROUP, INC.

/s/ Brian R. McLeod	/s/ William L. Brunson, Jr.
Brian R. McLeod Chief Financial Officer and Treasurer	William L. Brunson, Jr. President, Chief Executive Officer and Director

Date: March 26, 2010

POWER OF ATTORNEY

Know all by these present, that the undersigned hereby constitutes and appoints Brian R. McLeod, with full power of substitution and/or revocation, the undersigned's true and lawful attorney-in-fact: to execute for and on behalf of the undersigned, in the undersigned's capacity as a director of National Security Group, inc. (the "Company"), any and all forms (including, without limitation Form 10-K) required or desired to be executed by or on behalf of the Company pursuant to section 13 or 15(D) of the Securities Exchange Act of 1934, as amended, after said form has been approved by the Company's audit committee; to do and perform any and all acts for and on behalf of the undersigned which may be necessary or desirable to complete and execute any such Form and timely file such Form with the appropriate governmental authority (including, without limitation, the United States Securities and Exchange Commission) and any stock exchange or similar authority; and Take any other action of any type whatsoever in connection with the foregoing which, in the opinion of such attorney-in-fact, may be of benefit to, in the best interest of, or legally required by, the undersigned, it being understood that the documents executed by any such attorney-in-fact on behalf of the undersigned pursuant to this Power of Attorney shall be in such form and shall contain such terms and conditions as such attorney-in-fact may approve in such attorney-in-fact's discretion.

The undersigned hereby grants to each such attorney-in-fact full power and authority to do and perform any and every act and thing whatsoever requisite, necessary, or proper to be done in the exercise of any of the rights and powers herein granted, as fully to all intents and purposes as the undersigned might or could do if personally present, with full power of substitution or revocation, hereby ratifying and confirming all that such attorney-in-fact, or such attorney-in-fact's substitute or substitutes, shall lawfully do or cause to be done by virtue of this Power of Attorney and the rights and powers herein granted. The undersigned acknowledges that the foregoing attorneys-in-fact, and each of them, in serving in such capacity at the request of the undersigned, are not assuming, nor is the Company assuming, any of the undersigned's responsibilities to comply with section 13 or 15(D) of the Securities Exchange Act of 1934, as amended.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in their capacity as a Director of The National Security Group, Inc. on March 26, 2010.

SIGNATURE

/s/ Winfield Baird

/s/ Mickey L. Murdock

/s/ Fleming Brooks	/s/ Donald Pittman
/s/ Jack E. Brunson	/s/ Paul C. Wesch
/s/ William L. Brunson, Jr.	/s/ L. Brunson White
/s/ Fred D. Clark, Jr.	/s/ Walter P. Wilkerson
/s/ Frank B. O'Neil	

87