



North Coast Life

ANNUAL REPORT TO STOCKHOLDERS FOR 2001



Pictured is the front of your Company's Home Office Building at West 1116 Riverside Avenue in Spokane. This building, the former Elks Club, was designed by the noted architect Kirtland Cutter and was constructed between 1919 and 1921. The building is listed on the National Register of Historic Buildings, and is within the Riverside Historic District. Your Company occupies the upper level of the building. The first floor is leased to the Attorney General of the State of Washington.

DIRECTORS

Ronald D. Andrews
Thomas V. Atwater
Gavin J. Cooley

William C. Fix
Warren C. Heylman
Nicholas R. Knapton

Dennis E. Kraft
Douglas H. Ogden
C. Robert Ogden

Robert J. Ogden
Ronald R. Snyder

OFFICERS AND MANAGEMENT PERSONNEL

C. Robert Ogden, J.D.
President
Since 1965

Robert J. Ogden
Executive Vice President
Sales and Insurance Operations
Since 1989

Richard D. Hillier
Senior Field Vice President—Sales
California and the Southwest
Since 1978

Clifford D. Kutsch
Secretary—Director of
Agency Administration and
General Services
Since 1965

Gavin J. Cooley, CPA
Treasurer
Since 1990

Samuel C. Luke
Regional Vice President—Sales
Hawaii and the Pacific
Since 1985

Randy G. Thomas
Regional Vice President—Sales
Pacific Northwest
Since 1999

Delores J. Dressel, FLMI
Vice President—
Policy Service and Claims
Since 1971

Carol A. Maynard, FLMI
Vice President
and Senior Underwriter
Since 1980

David E. Thrans
Assistant Vice President
Computer Services and Operations
Since 1983

Christine D. Lyon, FLMI
Assistant Vice President
Program Analysis and Programming
Since 1984

Jay W. Townsend, FLMI, ACS
Assistant Vice President
Micro Services and Networks
Since 1985

Linda E. Butler, FLMI
Assistant Secretary
Stock Transfer and Word Processing
Since 1974

Robin L. Johnston, CPA
Assistant Treasurer
Since 1992

Diana L. Buchmann, FLMI
Director of Policy Service
Since 2000

Sharon G. Gustafson, FLMI
Director of Accounting
Since 1987

Gary L. Noland, M.D.
Medical Director
Since 1995

HIGHLIGHTS

	<u>2001</u>	<u>2000</u>
NET GAIN FROM OPERATIONS	\$ 938,653	\$ 905,822
PAID NEW LIFE INSURANCE	\$ 46,862,180	\$ 51,440,303
(FACE AMOUNT)		
INSURANCE IN FORCE	\$ 579,995,639	\$ 592,101,003
(FACE AMOUNT)		
ASSETS	\$ 87,031,247	\$ 83,434,101
ASSET RESERVES		
ASSET VALUATION RESERVE (AVR)	\$ 1,211,135	\$ 900,842
INTEREST MAINTENANCE RESERVE (IMR)	\$ 637,868	\$ 565,299
STATUTORY CAPITAL AND SURPLUS	\$ 5,685,573	\$ 5,998,498
RISK BASED CAPITAL RATIO	438.8%	574%
INVESTMENT RATE OF BONDS AND PREFERRED STOCK	8.44%	9.31%
AVERAGE SIZE LIFE CASE	\$ 60,003	\$ 69,986
(FACE AMOUNT)		
RETURN ON EQUITY	13.9%	10.10%

A LETTER FROM THE PRESIDENT

Your Company operated in 2001 at a record net gain from operations of \$938,653 for the year, which is the figure that will be quoted by the rating agency A. M. Best, and at a net income after the preferred stock dividends and capital gains and losses of \$470,826. In the “Analysis of Operations and Financial Statements” which appears later in this report, you will find that these results largely came from an increase in premium income, a reduction in death claims and from a decrease in the lapsation of policies. While death claims are considered a “non-controllable expense” (although we control claims to a considerable extent by careful underwriting), the increase in premium and decrease in lapsation were planned goals as a part of our strategy for the year.

While total insurance in force continued to decline and ended the year at \$579,995,639, we gained insurance in force during the last quarter of the year. Paid face amount sales of life insurance were down slightly from 2000 to \$46,862,180, but the number of cases both issued and submitted rose by 6% in number and about 6.5% in premium. Our average size life case declined from \$69,968 in 2000 to \$60,003 in 2001, the result of our having placed more of our Whole Life IV and Graded Benefit policies which we told you in our report last year that we intended to emphasize during 2001.

Significantly, lapsation of business in 2001 was almost exactly 50% of the lapsation in 2000. This is largely the result of our having terminated an agency in Los Angeles about which we reported to you last year, but also because we are selling more policies with smaller face amounts where it is likely that the sale is based more closely on need. The fact that our insurance in force increased during the fourth quarter also indicates that we have reached a turnaround point in our growth cycle.

The biggest challenge that we faced in 2001 was the rebuilding of our agency force and restoring growth in sales. At December 31, 2001, the Company had 222 General Agents and 35 Agents and Brokers, where at the same date in 2000 we had 174 General Agents and 31 Agents and Brokers, an increase in our sales manpower of 27.5% during 2001. The Company continued to tighten recruiting requirements in all territories. The fact that we increased the number of cases submitted and placed and increased the average policy premium indicates that our strategy is beginning to work. The Company increased market share in our senior/final expense products and sales of our principal whole life product, which is sold under the trademarked name “Versatile Life”, remained strong. We anticipate that in 2002 life sales will increase modestly by about 8% to 10%.

Annuity sales, however, showed a dramatic increase in 2001 with \$958,696 of annualized annuity premium as against \$375,645 in 2000. The life insurance industry has seen a shift in customer preference in the last few years toward asset accumulation products rather than pure insurance coverage. We have seen an additional emphasis on annuity products since the tragic events of September 11, 2001. Through March 5, 2002, the date of the writing of this letter, our submitted annuity premium for 2002 is \$725,834 as compared to \$93,215 in the same period of 2001. In addition, in 2001, we introduced our “Care” reversionary annuity plan which developed a steady growth from the time it was introduced.

Our “reversionary annuity” is a unique plan in the industry. It is an inexpensive policy which carries with it not only the death benefit paid in the event of the accidental death of the insured but also carries a rider providing an annuity to the surviving spouse to which can be added annuity benefits to pay the college expenses of children in the family. We believe that this unique product will be of considerable interest to the large population of “Generation X” with younger families. Please call our Home Office if you would like further information about this outstanding product.

At the end of 2001 we lowered the interest rates that we apply on our life and annuity products, an action which resulted from the fact that the Federal Reserve lowered interest rates in order to stimulate the recovery of the economy. We believe that the interest rates which we are now applying are competitive in the marketplace and provide us with a “spread” which gives us the proper profitability. During the year we continued to invest in corporate bonds and preferred stocks. Our investment activities will be discussed in a following section of this report under the heading of “Investments.”

You will note from the "Highlights" page just preceding this letter that our capital and surplus at December 31, 2001, was \$5,685,573, down about \$300,000 from the end of the previous year. At the end of September the surplus account had come down about \$440,000, so there was an improvement in the fourth quarter. The reductions in the surplus account come from several sources, and will be reviewed in detail in the section of this report headed "Analysis of Operations and Financial Statements." Briefly, over the last several years, at the instigation of the National Association of Insurance Commissioners, there has been a "recodification" of statutory accounting which made several important changes. Life insurance companies do not report their operations and earnings to the states on the basis of "Generally Accepted Accounting Principles," but on the basis of "Statutory Accounting." While GAAP would measure the going concern value of a company, statutory accounting is more concerned with the measurement of solvency on a current basis. This "recodification" made several important changes which affected our surplus negatively on a "one time" basis. For example, the amortization of the premium paid on bonds was shortened from the date of bond maturity to the date of call, which resulted in the movement of about \$200,000 from surplus to reserves. Assessments by the state Guaranty Associations were required to be written off more quickly at an additional accrual of \$52,722. Electronic data processing equipment life was shortened from ten years down to three which took roughly an additional \$73,000. And the accrual of unused vacation cost us \$50,000. In addition, in the fourth quarter we increased reserves relating to some of the bonds in our investment portfolio as a result of the negative impact of the September 11 events on the financial markets.

An important thing in 2001 was our renegotiation of a financial reinsurance treaty early in the year, extending the treaty from 2003 to 2005 with a payout schedule of approximately \$350,000 per year. Since 1992 we have been paying off approximately \$4.7 million of "surplus relief", which are funds received from a reinsurer to whom we ceded a large block of business in force. At the end of 2001 we had reduced the amount of surplus relief to \$1,410,229. When the balance is retired, which we expect to be at the end of 2005, this \$350,000 a year will flow into earnings.

During the year we wrote to you about the exercise of the warrants for the purchase of common stock. At December 31, 2000, 143,254 warrants had been exercised out of the 275,106 warrants issued in 1992. The warrants were not transferrable and some had lapsed because of stock transfers. At the beginning of January, 2001, there had been 66,867 warrants outstanding held by 180 stockholders. During the year only 1,025 warrants were exercised by a total of eleven people, which fell well within the parameters of a private offering. At the end of the year, then, the Company had 611,983 common shares outstanding with a par value of \$3.50 a share and 362,691 shares of preferred stock at a par value of \$1 per share. The warrants have now expired, and we were disappointed that more warrants were not exercised.

One of the most important measurements of our Company's strength is its Risk Based Capital ratio. The RBC ratio simply means having a large enough capital base to support the investment and insurance risks of the Company. Every company is required to maintain a Risk Based Capital ratio of at least 250%. Our RBC ratio at the end of 2001 was 438.8% which, while down from the 573.5% at the end of 2000, still compares favorably to the ratio at the end of 1999 which was 447% and to the 305.4% which was our measurement when the Risk Based Capital requirements were established in 1993.

Comments with respect to our sales plans and products, our investments, and an analysis of our operations and financial statements follow in other parts of this report, together with further comments on our plans for the future.

We look forward to a very good year in 2002

Sincerely yours,

C. Robert Ogden
President

INVESTMENTS

Our Company's increase of premium income during 2001 permitted us to expand our bond portfolio during the year. As of December 31, 2001, the Company's investment portfolio consisted of \$53,745,672 book value of bonds, which was up from \$49,480,855 at the end of 2000. During the year, however, we reduced our preferred stock portfolio to \$7,849,061, somewhat below the \$8,260,559 at the end of 2000. As interest rates declined during 2001 the difference between the market and book values of our bond portfolio narrowed and our preferred stock book values and market values became the same.

We are permitted to hold 10% of our assets in preferred stocks, and currently have some room to add to that segment of our portfolio which we anticipate doing early this year.

We believe that interest rates have already hit their low point for the year but we do not think that it is likely that the Federal Reserve will tighten interest rates before fall. At the time that this report is being written, in early March, evidence of strengthening in the economy is becoming apparent, according to the "Beige Book" of the Federal Reserve, but our observation is that the recovery in the west is spotty. California seems to have come through the recession in 2001 in far better shape than most of the surrounding states, which was not true a few years ago when California suffered from a reduction in defense spending and the closing of electronic manufacturing plants. Oregon has now suffered from the reduction of employment in electronic manufacturing, as have Nevada and Washington, and Washington state will also suffer from the reduction in employment at Boeing. Arizona, New Mexico and Colorado also have been affected by the downturn in the electronic industry. The economies of Montana, Idaho and Wyoming have slowed because farm and ranch products have been depressed. Hawaii is suffering from a drop in tourism.

2001 will be remembered as The Year of the Fed. The Federal Reserve cut the federal funds rate from 6.50% to 1.75% (a 73% decline) during the year. In percentage terms, this was the most the Fed has ever cut rates during a calendar year (going back to 1954 when the Fed's data begins). The September 11 attack tripled liquidity in the bond and stock markets, delaying a recovery in the economy which had gone into recession apparently in March of 2001. During the year there was a huge wave of refinancing of mortgages, and a large decline in energy prices which contributed to the recovery beginning late in the year. The attack on September 11 resulted in a sharp decline in travel and leisure spending, took its toll in consumer confidence, and resulted in increased spending on defense and security. The drop in consumer confidence, however, appears to have stabilized early in 2002. This confidence seems to be reflected in the life insurance industry in more concentration on asset accumulation products rather than on pure life insurance coverage. However, we believe that 2002 will prove to be a good year for the insurance industry.

The value of our bond and preferred stock portfolios moves inversely to interest rates. As interest rates came down, our portfolios recovered in market value. We do not see a rapid increase in interest rates this year, and we think that our portfolios will maintain their values and continue to recover as strength in the economy is reflected in corporate profits and the stock market moves slightly higher. During the year, therefore, we will continue to purchase corporate bonds of relatively long maturity and preferred stocks. We have mentioned before in these reports that our Company maintains a "Statement of Investment Philosophy" which authorizes the purchase of an equity portfolio in mutual funds in an amount of no more than \$1.25 million. The Board of Directors has not elected to establish such a portfolio because of conditions in the stock market, but that decision will be reviewed again in 2002.

We also maintain a mortgage loan portfolio which at year end 2001 was \$7,051,203, down from \$8,274,526 at the end of 2000 because of loan payoffs. We maintain an affiliation with R. J. Martin Mortgage Company to acquire individual mortgage loans in the immediate area of Spokane. Mortgages which we acquired during 2001 were all first mortgage residential loans in which the Company held approximately a 75% loan to value ratio with an average yield of about 10.5%. We have found good residential loans more difficult to acquire, and do not contemplate a highly aggressive effort to acquire mortgage loans this year.

We also maintain an investment of \$1,546,425 in a partnership interest in our Home Office building in Spokane and \$12,732,907 in policy loans and liens. Our policy loans are almost entirely at 1% above the rate of “excess interest” that we pay on our ordinary life policies (which currently is 5.5% plus a one-half percent bonus for policies which have been in force longer than 15 years). This “excess interest” is applied to the cash value of the policy. Our policies permit us to change the rate of “excess interest” to respond to economic conditions. Our policy loans will be made this year at a rate which is lower than we can invest money in bonds or preferred stock.

The Company obtained an average yield to maturity without consideration of early redemption of 8.44% on the roughly \$8.5 million of bonds and preferred stocks purchased during 2001. So far in 2002 we are averaging 8.35%. For our Company’s products to be profitable, we need a spread of approximately 200 to 250 basis points above the rate of “excess interest” which we apply to our products, so with our Versatile Life we need to have an investment return of about 7.5% to 8.0%. With annuities we need perhaps a larger margin of 250 to 300 points, and since we will be applying 5.35% on our basic Flexible Premium Annuities, we need to obtain a similar 7.85% to 8.35% yield. The yields which we are obtaining will give us the spreads which we need. We subscribe to a service which gives us a monthly analysis of the credited interest rates of 23 interest sensitive whole life products, 188 flexible premium deferred annuities and 263 single premium annuities with which we compete. We believe that the credited interest rates of our Company are currently favorably positioned against these competitors.

Your Company also held at the end of 2001 an amount of \$124,463 in “non-admitted assets.” These are assets which the Company is not allowed by the rules of statutory accounting to include as “admitted assets” for regulatory purposes. These assets include mortgages which are more than three months in arrears, commissions which we have advanced to agents (agents’ balances and loans) and the Company’s furniture, equipment and automobiles other than computer equipment. Our Company currently maintains a very low level of agents’ debit balances and loans. The Company’s partnership interest in West 1124 Riverside Avenue Partners, which owns one of the two connected buildings in which your Company’s home office is located, is a profitable partnership. Our Home Office building, of which we occupy only a part, is fully rented.



C. Robert Ogden
President

SALES, PRODUCTS AND PRODUCT DEVELOPMENT

Overview: Results Show Success of New Product Introductions

The year 2001 shows sales growth in new products recently introduced and a change in marketing sales mix of our “Versatile Life” interest-sensitive whole life product, the Company market leader. Overall, total life insurance sales increased in number of cases submitted and placed and increased in average policy premium with a lower per policy face amount. This is because of the continued increase in market share of our senior/ final expense products with the introduction of our Two Year Graded Life product during 2001, complementing our, “Peace of Mind for Tomorrow” or Whole Life IV plan, introduced a few years ago.

Versatile Life family market sales remain strong, but with less emphasis on higher face amounts accomplished from the use of 5-year, 10-year, 15-year or 20-year level term insurance riders that can more than double the face amount if needed. In the past few years, the additional term riders were used heavily by the Arakelyan agency for mortgage protection sales. That agency was terminated for poor persistency and selling practices, which was reported to you last year, resulting in the more typical use of our Versatile Life product line for traditional family protection and retirement savings.

There was a dramatic increase in annuity sales in 2001 attributed to increased marketing efforts from the Company’s first complete line of fixed interest-rate annuity products, made up of two flexible premium plans, four single premium deferred plans, and one single premium immediate annuity plan. The recently introduced single premium line of plans has greatly enhanced the ability of the Company to attract new agents and new sales in all annuity product lines. The “*Care*” reversionary annuity plan is also seeing steady growth and success in increasing sales. We have been especially pleased with this product’s growth in Guam and expect it to continue to build popularity in all territories.

Recruitment of Agents

Recruitment efforts in 2001 resulted in an increase in contracted General Agents, Associates and Brokers from 205 to 257, over a twenty-five percent increase. The largest area of growth is attributable to our new agency on the island of Guam, which I will discuss in more detail later. Recruitment efforts continue on a regular basis with a regional territory focus in the States here in the Northwest, in the Southwest, and in Hawaii and Guam, which also includes Saipan and the Commonwealth of the Northern Mariana Islands.

We continue to tighten our recruiting requirements in all territories, and every agent applying for a contract is checked for outstanding debit balances with other companies through Vector One, an online debit account reporting company similar in concept to MIB (Medical Information Bureau). The “quality not quantity” recruiting approach has measurably improved the persistency of new business we currently receive and has greatly reduced lapsation of policies. Our recruitment approach is to increase the agent count with agents writing a reasonably steady amount of quality business, without relying on a few agents writing a considerable amount of business that can be subject to poor persistency.

We recruit to North Coast Life by targeting direct mail to licensed life insurance agents in specific zip code areas. In 2001, our recruiting efforts focused in the Northwest States of Washington, Oregon, Idaho and Montana. In the Southwest, we concentrated in the inner valley areas of California, with Fresno, Bakersfield and Sacramento earlier in the year and the counties of Riverside and San Bernardino later in the year.

Sales - New Business Projections

Richard Hillier, Senior Field Vice President, works out of Chino, California, and is responsible for the recruitment and training of agents in our Southwest territory of California, Arizona, Nevada and New Mexico. We look for sales in Richard Hillier’s territory to have an increase in 2002 over 2001 by 10%, or between \$22 and \$25 million face amount placed.

Group Employees and Associates of Murray, Utah, works in the federal government employee and school district payroll deduction markets of Utah, Arizona and New Mexico, with consistent year after year sales. We will continue to see the same numbers in year 2002 with between \$15 and \$18 million face amount placed. For 2001, Group Employees placed 18.1 million face amount and has enjoyed increasing sales for several years now.

We also see continued growth locally in the states of Washington, Oregon, Idaho and Montana with Randy Thomas, Regional Vice President for the Northwest. Submitted sales in 2001 were over \$16 million face amount in this region, however, due to early detection of newly recruited agents that were not up to our standards and thus terminated, only \$8.5 million became placed. We expect to see sales continue to grow conservatively in this territory with around \$10 million face amount placed in 2002.

Other areas of potential increases in sales are the territories of Hawaii and Guam. We are developing a multi-agency presence on the island of Guam through our General Agent, Roger Surban, of Citadel Insurance Underwriters, Inc. Roger has teamed-up with several agencies on Guam to sell products for North Coast Life and just recently affiliated with an agency for expansion into Saipan, the largest island in the Commonwealth of the Northern Mariana Islands. We are beginning to receive a steady amount of sales and there is potential for a substantial increase. Sales in this region are just beginning, and a conservative sales goal for 2002 is \$5 million placed face amount.

A reasonable sales projection for year 2002 is \$55 million face amount placed. However, as explained earlier, face amount may not be the best projection of our continued growth, with premium and case count showing the company's significant growth in 2001 over the year 2000.

We intend to continue to emphasize our strategy of "controlled growth" by which we increase our sales while also increasing our surplus account. We believe that strong growth in our annuity sales, coupled with a relatively modest increase in life insurance sales will not result in a strain on surplus. During the last quarter of 2001 our insurance in force began to grow once again, and we look for continued growth through 2002.

Current Products

The overall increase in annuity sales can be attributed to our product development goal to build a complete line of fixed-interest rate annuity plans. Our past company success in the annuity market had focused on flexible premium annuities targeted towards the TSA market and other small, monthly savings plans that grow for retirement needs. Last year we added four Single Premium Deferred Annuity plans and a Single Premium Immediate Annuity designed to expand and "round-out" our line of annuity products, which also includes the two popular Flexible Premium Deferred Annuities. Sales of the new single premium annuities as well as the flexible premium annuities increased in year 2000, and dramatically increased in 2001. The marketing materials for the new single premium annuities called "*Annuity Portfolio*" have also been well received. We believe that fixed interest rate annuities will continue to have higher popularity in 2002 and sales will continue to reflect the increased marketing efforts of our completed annuity products line.

The Company market leader continues to be interest-sensitive whole life, distributed under the trademarked name "Versatile Life." The Versatile Life plans with term riders attached continue as our most popular sellers, however as discussed earlier, there is a more traditional use of the product for family protection needs and retirement goals with long-term cash values growth, which has resulted in a lower face amount average case size. The Versatile Life "family plan" marketing package, where one Versatile Life policy with one \$35 policy fee covers the entire family, remains our market leader. Product affordability for the "mom and pop" policyholder market that we serve, remains a focus of our product enhancement and development efforts.

Products Introduced in 2001

We introduced two new products early in 2001. The "*Care*" reversionary annuity plan was initially planned for release only in California. As a reminder, we had difficulty getting this product approved in our domicile state of Washington. The "*Care*" plan has since been approved in all states we are licensed in that do not require home state

approval first, which include Arizona, California, Colorado, Hawaii, Idaho, Wyoming, Guam and Saipan. Sales of the plan are steadily increasing in all areas with the strongest growth currently occurring in Guam.

Recruiting responses to North Coast Life from agents in the final expense senior market since the introduction of our "Peace of Mind for Tomorrow" WL-IV, Simplified Issue plan, have grown steadily. In addition to the WL-IV plan, our new Two Year Graded Life plan completes our senior market/final expense market product mix, which has shown good increased sales for 2001. The plan has a \$2,500 minimum to \$25,000 maximum face amount and pays 25% of the face amount on death in the first year, 50% in the second year and 100% thereafter. Full accidental death, however, would be paid from policy issue. This plan compliments our "WL-IV" simplified issue, short application plan which also has a \$2,500 minimum to \$25,000 maximum face amount. Both plans offer guaranteed premiums, cash values and death benefits. Because our "WL-IV" plan is designed to only insure people with health conditions through underwriting tables one through four, the Graded Death Benefit plan expands our senior market/final expense portfolio to offer a plan to insureds with health conditions exceeding four tables. Both plans target agents that specialize in the final expense senior market. Our agent direct mail recruiting brochure focuses on this market with these products, the family market with Versatile Life, the "Care" accidental death plan and mentions our term and annuity plans as well.

Conversion of Agency Software

Our agency software, which gives agents the ability to quote and illustrate all of our products on their own personal computer, is being rewritten at this time to be driven by Microsoft Windows. Our current agent software is a Microsoft DOS based system and has served us well up to now. We are finding new agents we recruit are familiar with and prefer Windows driven software, which has rapidly become the standard offered by other insurance companies. We have also been concerned that with the advancement of computer printers that also serve as fax and/or copy machines, the printing of our illustration software may not work properly unless the program is Windows driven.

The project is progressing well. The annuity programs are finished and the "Versatile Life" system rewrite is underway. This is our most complicated program and it is near completion. Once accomplished, the Whole Life and Term programs will follow and are much simpler to complete. We felt it was important to develop the most difficult program of Versatile Life first, and the results look to be a state of the art system. With the Windows system complete, the programs can also serve as models for our illustration needs over the Internet for both agents and individuals looking for interactive information, annuities and/or life insurance.

Internet

The company's web site found at www.nclife.com, has been updated extensively throughout year 2000 and 2001. Our long term goal for the Internet is to have it become an important part of our communication with prospects, policyholders, agents, stockholders, or anyone wanting company financial information, and the means of product sales both through request for agent consultation and sales directly by the Home Office.



Robert J. Ogden
Executive Vice President
Sales and Insurance Operations

ANALYSIS OF OPERATIONS AND FINANCIAL STATEMENTS

This discussion and analysis provides an assessment by management of the Company's current financial position and results.

Balance Sheet

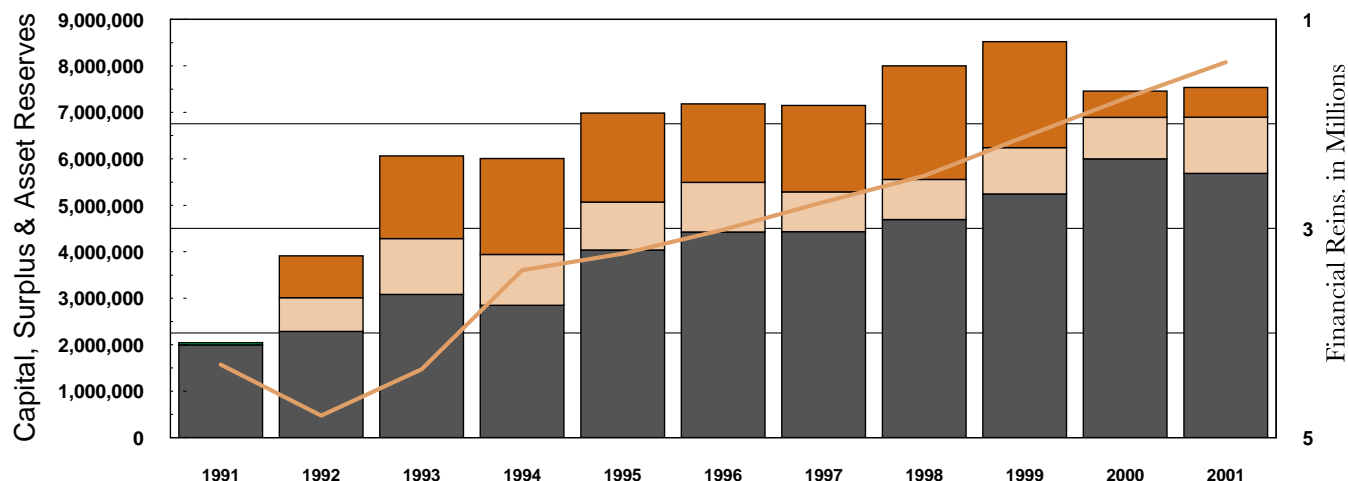
Capital and Surplus

The Company's capital and surplus decreased \$312,925 (5.2%), moving from \$5,998,498 at December 31, 2000 to \$5,685,573 at December 31, 2001. The decrease resulted generally from the effects of the mandatory adoption of accounting principles established under the Codification of Statutory Accounting Principles (see discussion under Codification of Statutory Accounting Principles below) together with operational items discussed herein.

The following graph depicts a ten-year history of the Company's statutory capital, surplus, asset reserves, and financial reinsurance balances.

NORTH COAST LIFE December 31, 2001

Statutory Capital, Surplus, Asset Reserves & Financial Reinsurance



	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
■ Capital & Surplus	1,994,586	2,288,115	3,084,117	2,849,048	4,036,913	4,426,109	4,433,340	4,693,490	5,242,983	5,998,498	5,685,573
□ AVR		724,958	1,200,909	1,096,748	1,030,656	1,065,891	855,516	861,356	998,741	894,362	1,211,135
■ IMR		900,096	1,776,857	2,061,489	1,919,128	1,689,954	1,860,057	2,447,682	2,279,345	565,299	637,868
□ MSVR	50,000										
— Financial Reins.	4,302,877	4,791,347	4,348,296	3,400,000	3,241,290	3,013,366	2,747,472	2,497,736	2,124,199	1,757,151	1,410,229
■ Percentages *	3.7%	6.5%	9.1%	8.8%	9.8%	9.7%	9.1%	9.8%	10.2%	8.9%	8.6%

* Percentages depict ratio of capital, surplus, & asset reserves to total assets

Despite a modest recent decline, the graph generally demonstrates strong aggregate growth even while the Company has aggressively paid down financial reinsurance balances.

Assets

The relative composition of the Company's investment portfolio was little changed during the year. Bond and preferred stock investments increased an aggregate \$3.9 million or 6.7%. The level of preferred stock investments at 9.0% of total assets is consistent with the Company's investment objectives, which call for an approximate level of 10%.

The market values of bond and preferred stock holdings are less than the carrying value on the Company's books as follows:

	Carry Value	Market Value	Excess/(Deficit)
Bonds	53,745,671	47,901,846	(5,843,825)
Preferred Stocks	7,849,061	7,737,355	(111,706)
Totals	61,594,732	55,639,201	(5,955,531)

Management is closely monitoring both the credit quality and market valuations of all of its investments. Both the credit issues and the deficit in market values may be viewed, at least in part, as cyclical. For instance, 1999 was considered the second worst year for the bond market since 1973 and the long end of the yield curve for corporate securities, similar to those held by the Company, has recovered only moderately since that time. The national economic downturn is also seen as contributing to downward pressure on the credit quality of these securities. Another potential mitigating factor is that the Company has not observed significant market pressure to increase credited rates on its products to levels which would materially reduce Company profitability; in other words, the investment income earned on the Company's invested assets has been sufficient for the Company to maintain competitive rates on its products, (see also discussion of IMR and AVR reserves under Liabilities).

Holdings of mortgage loans on real estate dropped 14.8% from \$8.3 to \$7.1 million. The decrease resulted primarily from a high number of loan pay-offs due to the availability of substantially lower interest rates on new loans and the continued seasoning of the Company's loan portfolio. The loans are of a very small size, averaging approximately \$41,478 of admitted value for the 170 loans in the portfolio. 168 of the loans are first-lien residential mortgages and two of the loans are first-lien multi-family residential mortgages (small apartment buildings). The Company anticipates a continuing reduction in the levels of its mortgage loan investments due to payoffs.

The Company made loan purchases during the year aggregating \$408,471 of principal and an average yield of approximately 10.8%. The Company does not anticipate increasing the level of these secondary market purchases of loan interests due to highly competitive market conditions. These conditions make it difficult to obtain sufficiently high yields to justify the increased administration costs without increasing default and other risk parameters.

The Company holds no derivative investments, and no CMOs or other derivative real estate investments.

Liabilities

The majority of the Company's liabilities are comprised of Policy Reserves (98%). These reserves showed an increase of 4.8%. This increase is somewhat higher than in recent years and generally reflects an increasingly healthy level of premiums together with decreases in surrenders and other policy benefits.

Claims Payable decreased substantially from \$421,928 to \$149,374 - this represents an inconsequential timing difference only. Policy dividends and premiums paid in advance were constant while other policy liabilities rose from \$42,794 to \$187,294 based upon policy remittances pending allocation and amounts payable for securities purchases.

The Interest Maintenance Reserve (IMR) increased 12.8% to \$637,868. The increase results from realized gains on the sale of IMR related fixed income securities. Two years previous, the IMR was reduced approximately 75% as the Company disposed of many securities whose market values had decreased generally as a result of fluctuations in market rates of interest.

The IMR stands at approximately .8% of cash and invested assets. At this level, management believes the IMR is only marginally adequate to account for the potential interest rate and credit risk associated with the Company's bond and preferred stock investments (see earlier discussion of Company assets).

The Company's Asset Valuation Reserve (AVR) increased 34.4% to \$1,211,135. The increase primarily results from increased reserve contributions relative to the higher levels of Company securities with ratings below investment grade. Management anticipates the AVR will decrease somewhat in coming years in direct proportion to decreased risk from invested assets (see discussion of Company assets). For instance, management anticipates that as the national economy begins to recover, many of the Company's securities will be positively impacted and hence upgraded, thereby reducing AVR requirements.

Other non-operating items affecting the Company's capital and surplus accounts include changes in non-admitted assets, continued payment on the Company's 10% Cumulative Convertible preferred stock, and pay-downs in the Company's financial reinsurance balance.

Results of Operations – Discussion

Income

The Company's premium income from life and annuity policies for December 31, 2001 was 7.9% higher than the preceding year as follows:

	<u>12/31/01</u>	<u>12/31/00</u>
Life Premiums:		
First-Year	585,649	476,323
Renewal	<u>5,341,613</u>	<u>5,473,951</u>
Total	5,927,262	5,950,274
Annuity Premiums	1,677,905	1,093,597
Accident & Health	<u>3,872</u>	<u>3,619</u>
Total Gross Premiums	7,609,039	7,047,490

The increase in first-year life premiums is an indication that the Company's slate of new and existing products are viable in the increasingly competitive marketplace.

Renewal premiums decreased 2.4%. Although the decrease is relatively small, management is intensifying its review of persistency records and taking other action to assure the highest level of policy retention.

Annuity premiums increased a very strong 53.4% as the Company's slate of annuity products began to take hold and demonstrate viability in the very competitive marketplace.

Expenses

Death benefits decreased 56.1% from \$1,379,047 to \$605,039. Excluding the effects of financial reinsurance the decrease was 37.1% moving from \$2,149,926 to \$1,352,092. (The aggregate net effect of the financial reinsurance treaty is typically zero - accordingly, it can be useful to exclude the effects of such reinsurance from items such as death claims and surrender benefits to better understand the net impact of such items on the Company's net income.) The general trend in death benefits, including the current decrease, continues to be favorable.

The following table shows the Company's relatively constant and generally favorable death claims experience over a five-year period. The claim amounts are shown net of policy reserves and ordinary reinsurance but exclude the effects of financial reinsurance.

	2001	2000	1999	1998	1997
1 st Quarter	153,233	207,156	334,523	309,732	226,693
2 nd Quarter	151,396	267,709	389,513	273,343	344,466
3 rd Quarter	411,624	271,807	134,547	310,474	406,948
4 th Quarter	189,462	397,275	230,349	227,681	92,896
Annual Totals	905,715	1,143,947	1,088,932	1,121,230	1,071,003

General expenses at \$2.3 million were \$92,447 (4.2%) higher than the prior total. After taking into account increased expenses associated with the adoption of Codified Accounting Principles, these expenses were generally in line with levels budgeted by management. (See Codification of Statutory Accounting Principles.)

The Company has continued to follow a plan for aggressive utilization of new computer technologies and other administrative improvements. This program has allowed the Company to reduce personnel and related costs even while maintaining similar or improved levels of service.

Consistent with the prior year ending December 31, 2000, the Company has not incurred Federal income taxes in 2001. This results in part from net operating loss and other tax attribute carry forwards. In addition, in the fourth quarter of 2000 the Company discontinued its practice of allocating federal income tax to gains and losses flowing into the Company's Interest Maintenance Reserve from the disposition of fixed income securities.

Examination Reports

The Company is presently being examined by the Department of Insurance for the State of Washington for the years 1996 through 2000. As of March 8, 2002, the Examination field work appears to have been completed. At this time, management is unaware of the need for any material adjustments to the Company's books resulting from this examination in progress. It is expected that the examination report will be available during the year 2002. The last completed examination of the Company was for the period July 1, 1993 through December 31, 1995 and was conducted by the Department of Insurance for the State of Washington. The examination was finalized effective December 31, 1997. No adjustments to the Company's books resulted from the examination.

Codification of Statutory Accounting Principles:

A long-term project to revise and generally update existing statutory accounting guidance was recently completed. Known as the “Codification of Statutory Accounting Principles”, these changes become effective January 1, 2001. Accordingly, effective with the first quarter of 2001, the Company adopted the accounting principles established under “Codification”.

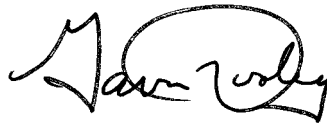
The new accounting principles are enumerated in The Statements of Statutory Accounting Principles (SSAP’s) included in the Accounting Practices and Procedures Manual published by the NAIC. A summary of the material changes as they have applied to the Company includes the following:

- Under SSAP No. 11, vacation expense has been accrued as a compensated absence. The cumulative effect on prior years was a decrease to surplus of \$53,670. The current year change in the accrual amounted to a decrease of \$5,808 as of December 31, 2001.
- Under SSAP No. 16, the depreciable lives of the Company’s EDP equipment were decreased to 3 years from the previous estimate of 10 years. This resulted in additional depreciation expense of approximately \$73,000.
- Under SSAP No. 46, the Company revised its accounting for its affiliate - W. 1124 Riverside Partners. Prior to Codification, the Company’s share of income/loss in the affiliate was recorded as a realized gain or loss component of investment income. Under Codification, these gains/losses will now be included in the Change in Unrealized Gain/Loss segment of surplus.
- SSAP No. 40, Real Estate Investments, requires the Company to carry all real estate at lower-of-cost-or-market, rather than non-admitting the amounts above market as done previously. This resulted in an increase in prior years’ surplus of \$948.
- SSAP No. 26, Bonds, requires the Company to amortize bonds containing call provisions to either the call or maturity date, whichever produces the lowest asset value. The cumulative effect on prior years was a decrease to surplus of \$200,000.
- SSAP No. 52, Deposit-Type Contracts, requires the Company to record amounts received on deposit-type contracts to be recorded directly to policy reserves rather than recorded as revenue. The effect of is to reclassify amounts received from revenue directly to the reserves but does not increase or decrease Company surplus.
- SSAP No. 35, Guaranty Fund and other Assessments, requires the Company to accrue Guaranty Fund assessments when the insolvency occurs. Previously, companies often accrued such amounts at the time of assessment resulting in a general deferral of amounts due. Guaranty fund assessments totaling \$167,753 are accrued as of year-end 2001.

Other changes have been made to comply with the provisions of Codification which have not had a material effect on the Company’s financial statements.

The total impact from Codification discussed above, has had a direct or timing impact on the Company's Capital and Surplus accounts totaling approximately \$488,000.

The financial statements displayed and discussed herein are prepared on the basis of Statutory Accounting Principles (also known as regulatory accounting). The Company also prepares its statements annually on the basis of Generally Accepted Accounting Principles (GAAP). The company's Statutory and GAAP basis financial statements are regularly posted on the Company's web site: www.nclife.com. In addition, a more detailed discussion of the Company's financial operations is also posted on the site (labeled "Management's Discussion and Analysis").

A handwritten signature in black ink, appearing to read "Gavin Cooley". The signature is stylized with a large, rounded initial "G" and a cursive "Cooley".

Gavin J. Cooley, CPA
Treasurer

LOOKING AHEAD

At December 31, 2001, we had 211 common stockholders and 297 preferred stockholders. At that time, also, as mentioned earlier in this report, we were represented by 222 General Agents and 35 Agents and Brokers, an increase in our sales manpower of 27.5% during 2001. We intend to continue to recruit aggressively this year. We have applied for readmission in the state of Alaska, and expect that to be accomplished during 2002. We also will continue to operate in the twelve western states of Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington and Wyoming in which we are currently licensed. We also are admitted to do business in Guam and the Commonwealth of the Northern Marianas (which principally is Saipan) where we have been developing increasing sales.

The 2000 census showed a total population in the twelve states in which we are admitted of 62,571,000. California remains the largest state with 33,871,648 (54%), Washington is second with 5,894,121, Arizona is third with 5,130,632, Colorado is fourth with 4,301,261, and Oregon is fifth with 3,421,399. 39.5% of our sales in 2001 were in California. Dick Hillier, our Senior Field Vice President, is based in Chino, California, and covers for us the states of California, Arizona, New Mexico and Nevada. Randy Thomas has been successfully recruiting in the Northwest, especially around Spokane, but covers the states of Washington, Oregon, Idaho and Montana. Randy also will cover Alaska when we are admitted there. Utah and Wyoming are covered by our General Agent, Ken Peterson, who is based in the Salt Lake area. Ken's agency also does business in Nevada, Arizona and New Mexico. Colorado is covered out of the Home Office by our Executive Vice President for Sales and Insurance Operations, Rob Ogden.

Our Company's agency software, which gives our agents the ability to quote and illustrate all of our products on their own personal computer, is being converted in-house to be driven by Microsoft Windows. Our current agency software is a Microsoft DOS based system. We have found that the new computer printers which also serve as fax or copy machines may not print our illustrations properly unless the program is Windows driven. The new Windows programs also will become a base for our illustration needs over the Internet.

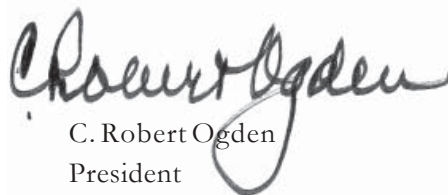
Our Company's website, which you can find at www.nclife.com, has been updated extensively and many of our policyholder service forms are now available for download and printing thus saving mailing expense and time to the policyholder. This year we expect to include a secure site for access using a password and social security number for policyholders to view pertinent information about their policies. We also are working to add to our web domain a secure site for access to agent commission statements and the status of application requirements still pending in underwriting. We continue to work toward being able to offer products for sale over the Internet, including the possibility of direct sales from the Home Office.

We have mentioned earlier in this report that we anticipate that our life insurance sales should increase this year approximately 8 to 10%, which we feel that we can do without incurring any strain on surplus. Continuation of the rapid growth of our annuity sales is more difficult to predict. Our new annuity products, however, are taking hold well, and we anticipate that annuity sales will remain strong.

Our staff and our agency force are responding well to the Company's greater strength and from the recent affirmation of our A. M. Best rating. We are meeting the challenge of rebuilding our agency operation. Sales are growing again. We look forward to a good year in 2002.

To each agent, employee, officer and member of our Board of Directors, and to each of you as our stockholders, I extend my sincere appreciation and thanks.

Sincerely yours,



C. Robert Ogden
President

NORTH COAST LIFE INSURANCE COMPANY
Spokane, Washington

BALANCE SHEET - STATUTORY BASIS

<u>ASSETS</u>	December 31, 2001 (Unaudited)	December 31, 2000
Ledger and Non-Ledger Assets:		
Bonds (market: \$47,901,848/\$43,911,326)	\$53,745,672	\$49,480,855
Preferred stocks: (market: \$7,737,355/\$7,612,152)	7,849,061	8,260,559
Mortgages (residential)	7,051,203	8,274,526
Real estate owned (REO)	149,054	91,539
Other invested assets	1,565,575	1,588,827
Policy loans and liens	12,732,907	12,045,317
Deposits and cash	33,347	(11,666)
Agents' balances and loans	23,672	46,092
Furniture, equipment and autos	63,371	64,837
Computer equipment	28,055	83,262
Premiums deferred & uncollected	2,222,399	2,221,518
Investment income due & accrued	1,310,672	1,150,540
Amounts receivable:		
Reinsurance	1,361	2,118
Other	367,968	292,144
Guaranty Association assessments	11,393	24,710
Total Ledger and Non-Ledger Assets	<u>87,155,710</u>	<u>83,615,178</u>
Non-Admitted Assets included above:		
Fixed income investments	0	0
Mortgages, REO and related	37,420	70,148
Agents' balances and loans	23,672	46,092
Furniture, equipment and autos	63,371	64,837
Subtotal	<u>124,463</u>	<u>181,077</u>
NET ADMITTED ASSETS	<u>\$87,031,247</u>	<u>\$83,434,101</u>
 <u>LIABILITIES, CAPITAL AND SURPLUS</u> 		
Policy Liabilities:		
Policy reserves	\$78,295,531	\$73,122,731
Claims payable	149,374	421,928
Policy dividends & coupons	5,500	318,197
Premiums paid in advance	64,810	1,335,321
Other policy liabilities	187,294	42,794
Total Policy Liabilities	<u>78,702,509</u>	<u>75,240,971</u>
General Liabilities:		
Unearned investment income	345,724	313,074
Accrued taxes	172,773	165,365
Accrued general expenses	111,082	77,658
Preferred stock dividend payable	90,673	90,673
Other amounts payable	73,910	81,721
Total General Liabilities	<u>794,162</u>	<u>728,491</u>
TOTAL LIABILITIES	<u>79,496,671</u>	<u>75,969,462</u>
Asset Reserves:		
Interest Maintenance Reserve	637,868	565,299
Asset Valuation Reserve	1,211,135	900,842
Total Asset Reserves	<u>1,849,003</u>	<u>1,466,141</u>
Capital & Surplus		
Capital Stock	7,645,062	7,639,936
Surplus	(1,959,489)	(1,641,438)
Total Capital & Surplus	<u>5,685,573</u>	<u>5,998,498</u>
TOTAL LIABILITIES, CAPITAL & SURPLUS	<u>\$87,031,247</u>	<u>\$83,434,101</u>

NORTH COAST LIFE INSURANCE COMPANY
Spokane, Washington

CONDENSED SUMMARY OF OPERATIONS AND COMPARATIVE REPORT - STATUTORY BASIS

Through December 31, 2001

	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>
INCOME:					
Gross premium income	\$ 7,609,039	\$ 7,047,490	\$ 7,017,500	\$ 8,200,298	\$ 8,845,696
Less reinsurance	(1,537,403)	(1,564,840)	(1,920,939)	(1,776,418)	(2,290,401)
Policy dividends, coupons and supplementary contracts .	0	126,686	116,481	326,873	140,590
Investment income & IMR, net	6,304,646	6,372,411	6,328,206	6,219,335	6,070,005
Real estate income, net	(40,818)	38,303	(49,283)	(34,505)	(65,769)
Reinsurance commissions & reserve adjustments	1,158,056	1,136,822	933,641	1,332,913	1,597,190
Other income	0	0	0	0	0
Total operating income	<u>13,493,520</u>	<u>13,156,872</u>	<u>12,425,606</u>	<u>14,268,496</u>	<u>14,297,311</u>
OPERATING EXPENSES & RESERVES:					
Increases in policy reserves	2,891,177	237,667	1,257,883	2,481,890	3,664,961
Policy dividends, coupons and supplementary contracts .	86,077	153,062	205,651	137,032	88,785
Interest and adjust. on policy, deposit and other funds . . .	98,848	0	0	0	0
Policy benefits	3,991,578	6,577,479	4,858,189	5,504,936	4,586,070
Commissions	792,627	821,690	1,011,177	1,071,930	980,817
General expenses	2,300,401	2,207,954	2,244,782	2,251,674	2,367,693
Taxes, licenses & fees	286,378	295,955	372,291	196,964	239,362
Premium loading increases/(decreases)	14,899	(66,545)	(43,257)	31,461	84,228
Interest on reserve deposits	2,092,882	2,023,788	1,941,021	1,883,843	1,837,559
Total operating expenses & reserves	<u>12,554,867</u>	<u>12,251,051</u>	<u>11,847,736</u>	<u>13,559,730</u>	<u>13,849,475</u>
NET GAIN/(LOSS) FROM OPERATIONS	938,653	905,822	577,870	708,766	447,836
Realized capital gains/(losses)	72,411	(1,971,354)	(53,709)	530,097	293,453
(Gains)/losses transferred to the IMR	(177,546)	1,595,230	38,232	(716,746)	(298,942)
NET INCOME	<u>\$ 833,518</u>	<u>\$ 529,697</u>	<u>\$ 562,393</u>	<u>\$ 522,117</u>	<u>\$ 442,347</u>
Paid ordinary sales	46,862,180	51,440,303	96,055,238	108,151,335	92,765,789
In force at end of year	579,995,639	592,101,003	631,399,003	646,820,402	625,395,123
Total admitted assets	\$ 87,031,247	\$ 83,434,101	\$ 83,808,089	\$ 81,564,555	\$ 78,189,503

SURPLUS ACCOUNT - STATUTORY BASIS	December 31, <u>2001</u>	December 31, <u>2000</u>
CAPITAL AND SURPLUS DECEMBER 31, PREVIOUS YEAR	\$5,998,498	\$5,242,983
Gain from operations	938,653	905,822
Net Realized capital gains or (losses)	72,411	(1,971,354)
Less gains to Interest Maintenance Reserve	(177,546)	1,595,230
(Increase)/decrease in Asset Valuation Reserve	(310,293)	97,899
(Increase)/decrease in non-admitted mortgages and real estate	25,996	97,693
(Increase)/decrease in non-admitted stocks	0	0
(Increase)/decrease in non-admitted other invested assets	1,217	1,571
Net (increase)/decrease in agents' balances and other non-admitted items	7,751	78,396
(Increase)/decrease in net unrealized capital gains (losses)	86,097	
Cumulate effect of changes in accounting principles	(252,722)	
Dividends paid on Company preferred stock	(362,692)	(362,694)
Paydown of financial reinsurance balance	(346,922)	(367,048)
Exercise of common stock directed warrants	5,125	680,000
CAPITAL AND SURPLUS, CURRENT PERIOD	<u>\$5,685,573</u>	<u>\$5,998,498</u>



North Coast Life - THIRTY-SEVENTH ANNUAL REPORT

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