PROTECTIVE LIFE CORP
Form 10-Q
November 04, 2011
Table of Contents

# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D. C. 20549**

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# FORM 10-Q

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

**For the quarterly period ended September 30, 2011**

**or**

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

**For the transition period from to**

**Commission File Number 001-11339**

# Protective Life Corporation

(Exact name of registrant as specified in its charter)

| **Delaware** | **95-2492236** |
| --- | --- |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification Number) |

**2801 Highway 280 South**

**Birmingham, Alabama 35223**

(Address of principal executive offices and zip code)

**(205) 268-1000**

(Registrant s telephone number, including area code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes **x** No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes **x** No o

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

| Large accelerated filer **x** | Accelerated Filer o |
| --- | --- |
| Non-accelerated filer o | Smaller Reporting Company o |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No **x**

Number of shares of Common Stock, $0.50 Par Value, outstanding as of October 25, 2011: 82,812,088

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**QUARTERLY REPORT ON FORM 10-Q**

**FOR QUARTERLY PERIOD ENDED SEPTEMBER 30, 2011**

**TABLE OF CONTENTS**

**PART I**


| | | **Page** |
|---|---|---|
| Item 1. | Financial Statements (unaudited): | |
| | Consolidated Condensed Statements of Income For The Three and Nine Months Ended September 30, 2011 and 2010 | 3 |
| | Consolidated Condensed Balance Sheets as of September 30, 2011 and December 31, 2010 | 4 |
| | Consolidated Condensed Statement of Shareowners Equity For The Three Months Ended March 31, 2011, June 30, 2011, and September 30, 2011 | 5 |
| | Consolidated Condensed Statements of Cash Flows For The Nine Months Ended September 30, 2011 and 2010 | 7 |
| | Notes to Consolidated Condensed Financial Statements | 8 |
| Item 2. | Management s Discussion and Analysis of Financial Condition and Results of Operations | 45 |
| Item 3. | Quantitative and Qualitative Disclosures About Market Risk | 106 |
| Item 4. | Controls and Procedures | 107 |


**PART II**


| | | |
|---|---|---|
| Item 1A. | Risk Factors and Cautionary Factors that may Affect Future Results | 108 |
| Item 2. | Unregistered Sales of Equity Securities and Use of Proceeds | 113 |
| Item 6. | Exhibits | 114 |
| | Signature | 115 |

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**CONSOLIDATED CONDENSED STATEMENTS OF INCOME**

(Unaudited)

| | For The Three Months Ended September 30, 2011 | For The Three Months Ended September 30, 2010 | For The Nine Months Ended September 30, 2011 | For The Nine Months Ended September 30, 2010 |
|---|---|---|---|---|
| | (Dollars In Thousands, Except Per Share Amounts) | | | |
| **Revenues** | | | | |
| Premiums and policy fees | $ 696,978 | $ 640,265 | $ 2,079,907 | $ 1,948,278 |
| Reinsurance ceded | (326,967) | (334,040) | (1,023,023) | (1,019,598) |
| Net of reinsurance ceded | 370,011 | 306,225 | 1,056,884 | 928,680 |
| Net investment income | 462,926 | 429,548 | 1,355,924 | 1,264,045 |
| Realized investment gains (losses): | | | | |
| Derivative financial instruments | (97,816) | (94,034) | (145,495) | (236,994) |
| All other investments | 138,230 | 110,787 | 201,619 | 226,390 |
| Other-than-temporary impairment losses | (6,259) | (12,898) | (37,912) | (71,437) |
| Portion recognized in other comprehensive income (before taxes) | (3,570) | 5,283 | 12,933 | 35,155 |
| Net impairment losses recognized in earnings | (9,829) | (7,615) | (24,979) | (36,282) |
| Other income | 75,859 | 58,190 | 235,292 | 161,134 |
| Total revenues | 939,381 | 803,101 | 2,679,245 | 2,306,973 |
| **Benefits and expenses** | | | | |
| Benefits and settlement expenses, net of reinsurance ceded: (three months: 2011 - $208,720; 2010 - $308,594; nine months: 2011 - $878,991; 2010 - $971,061) | 592,792 | 549,567 | 1,680,714 | 1,582,233 |
| Amortization of deferred policy acquisition costs and value of business acquired | 83,782 | 42,386 | 237,833 | 146,761 |
| Other operating expenses, net of reinsurance ceded: (three months: 2011 - $48,924; 2010 - $48,851; nine months: 2011 - $142,994; 2010 - $142,932) | 131,604 | 104,151 | 382,127 | 305,246 |
| Total benefits and expenses | 808,178 | 696,104 | 2,300,674 | 2,034,240 |
| **Income before income tax** | 131,203 | 106,997 | 378,571 | 272,733 |
| Income tax expense | 42,589 | 36,626 | 129,127 | 91,412 |
| **Net income** | 88,614 | 70,371 | 249,444 | 181,321 |
| Less: Net income (loss) attributable to noncontrolling interests | | (77) | 245 | (277) |
| **Net income available to PLC s common shareowners(1)** | $ 88,614 | $ 70,448 | $ 249,199 | $ 181,598 |
| | | | | |
| Net income available to PLC s common shareowners - basic | $ 1.05 | $ 0.81 | $ 2.90 | $ 2.10 |
| Net income available to PLC s common shareowners - diluted | $ 1.03 | $ 0.80 | $ 2.86 | $ 2.07 |
| Cash dividends paid per share | $ 0.16 | $ 0.14 | $ 0.46 | $ 0.40 |
| | | | | |
| Average shares outstanding - basic | 84,722,232 | 86,603,569 | 85,883,669 | 86,555,761 |
| Average shares outstanding - diluted | 86,004,571 | 87,701,592 | 87,152,812 | 87,640,221 |

(1) Protective Life Corporation ( PLC )

See Notes to Consolidated Condensed Financial Statements

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**CONSOLIDATED CONDENSED BALANCE SHEETS**

(Unaudited)

| | As of | | | |
|---|---|---|---|---|
| | September 30, 2011 | | December 31, 2010 | |
| | (Dollars In Thousands) | | | |
| **Assets** | | | | |
| Fixed maturities, at fair value (amortized cost: 2011 - $26,139,017; 2010 - $24,002,893) | $ | 27,855,004 | $ | 24,676,939 |
| Equity securities, at fair value (cost: 2011 - $336,722; 2010 - $349,605) | | 327,802 | | 359,412 |
| Mortgage loans (2011 and 2010 includes: $875,096 and $934,655 related to securitizations) | | 5,377,977 | | 4,892,829 |
| Investment real estate, net of accumulated depreciation (2011 - $1,404; 2010 - $1,200) | | 27,495 | | 25,340 |
| Policy loans | | 880,203 | | 793,448 |
| Other long-term investments | | 284,550 | | 276,337 |
| Short-term investments | | 80,387 | | 352,824 |
| Total investments | | 34,833,418 | | 31,377,129 |
| Cash | | 332,487 | | 264,425 |
| Accrued investment income | | 363,548 | | 329,078 |
| Accounts and premiums receivable, net of allowance for uncollectible amounts (2011 - $3,855; 2010 - $4,330) | | 60,008 | | 58,580 |
| Reinsurance receivables | | 5,645,080 | | 5,608,029 |
| Deferred policy acquisition costs and value of business acquired | | 4,000,099 | | 3,851,743 |
| Goodwill | | 112,434 | | 114,758 |
| Property and equipment, net of accumulated depreciation (2011 - $133,419; 2010 - $130,576) | | 45,997 | | 39,386 |
| Other assets | | 201,516 | | 169,664 |
| Income tax receivable | | 11,142 | | 45,582 |
| Assets related to separate accounts | | | | |
| Variable annuity | | 5,947,391 | | 5,170,193 |
| Variable universal life | | 470,283 | | 534,219 |
| **Total assets** | $ | 52,023,403 | $ | 47,562,786 |
| **Liabilities** | | | | |
| Policy liabilities and accruals | $ | 21,909,724 | $ | 19,713,392 |
| Stable value product account balances | | 2,827,862 | | 3,076,233 |
| Annuity account balances | | 10,975,016 | | 10,591,605 |
| Other policyholders funds | | 575,056 | | 578,037 |
| Other liabilities | | 1,196,554 | | 926,201 |
| Mortgage loan backed certificates | | 32,471 | | 61,678 |
| Deferred income taxes | | 1,415,904 | | 1,022,130 |
| Non-recourse funding obligations | | 414,800 | | 532,400 |
| Reverse repurchase borrowings | | 157,103 | | |
| Debt | | 1,495,000 | | 1,501,852 |
| Subordinated debt securities | | 524,743 | | 524,743 |
| Liabilities related to separate accounts | | | | |
| Variable annuity | | 5,947,391 | | 5,170,193 |
| Variable universal life | | 470,283 | | 534,219 |
| Total liabilities | | 47,941,907 | | 44,232,683 |
| **Commitments and contingencies - Note 8** | | | | |
| **Shareowners equity** | | | | |

| | | | | |
|---|---|---|---|---|
| Preferred Stock, $1 par value, shares authorized: 4,000,000; Issued: None | | | | |
| Common Stock, $.50 par value, shares authorized: 2011 and 2010 - 160,000,000; shares issued: 2011 and 2010 - 88,776,960 | | 44,388 | | 44,388 |
| Additional paid-in-capital | | 594,084 | | 586,592 |
| Treasury stock, at cost (2011 - 5,964,872 shares; 2010 - 3,108,983 shares) | | (83,549) | | (26,072) |
| Retained earnings | | 2,642,860 | | 2,432,925 |
| Accumulated other comprehensive income (loss): | | | | |
| Net unrealized gains (losses) on investments, net of income tax: (2011 -$523,401; 2010 - $195,096) | | 972,031 | | 362,321 |
| Net unrealized (losses) gains relating to other-than-temporary impaired investments for which a portion has been recognized in earnings, net of income tax: (2011 - $(14,784); 2010 - $(5,223)) | | (27,455) | | (9,700) |
| Accumulated loss - derivatives, net of income tax: (2011 - $(5,408); 2010 - $(6,355)) | | (10,044) | | (11,802) |
| Postretirement benefits liability adjustment, net of income tax: (2011 -$26,966; 2010 - $(25,612)) | | (50,080) | | (47,565) |
| Total Protective Life Corporation s shareowners equity | | 4,082,235 | | 3,331,087 |
| Noncontrolling interest | | (739) | | (984) |
| Total equity | | 4,081,496 | | 3,330,103 |
| **Total liabilities and shareowners equity** | $ | 52,023,403 | $ | 47,562,786 |

See Notes to Consolidated Condensed Financial Statements

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**CONSOLIDATED CONDENSED STATEMENTS OF SHAREOWNERS EQUITY**

(Unaudited)

| | Common Stock | Additional Paid-In-Capital | Treasury Stock | Retained Earnings | Accumulated Other Comprehensive Income (Loss) Net Unrealized Gains / (Losses) on Investments | Accumulated Gain / (Loss) Derivatives | Minimum Pension Liability Adjustments | Total Protective Life Corporation s shareowners equity | Non controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|---|---|---|
| | (Dollars In Thousands) | | | | | | | | | |
| Balance, December 31, 2010 | $ 44,388 | $ 586,592 | $ (26,072) | $ 2,432,925 | $ 352,621 | $ (11,802) | $ (47,565) | $ 3,331,087 | $ (984) | $ 3,330,103 |
| Net income for the three months ended March 31, 2011 | | | | 67,517 | | | | 67,517 | (51) | 67,466 |
| Change in net unrealized gains/losses on investments (net of income tax - $17,907) | | | | | 33,263 | | | 33,263 | | 33,263 |
| Reclassification adjustment for investment amounts included in net income (net of income tax - $(3,054)) | | | | | (5,678) | | | (5,678) | | (5,678) |
| Change in net unrealized gains/losses relating to other-than-temporary impaired investments for which a portion has been recognized in earnings (net of income tax $(3,608)) | | | | | (6,700) | | | (6,700) | | (6,700) |
| Change in accumulated gain (loss) derivatives (net of income tax - $3,621) | | | | | | 6,724 | | 6,724 | | 6,724 |
| Reclassification adjustment for derivative amounts included in net income (net of income tax - $(361)) | | | | | | (671) | | (671) | | (671) |
| Change in postretirement benefits liability adjustment (net of income tax - $(451)) | | | | | | | (838) | (838) | | (838) |
| Comprehensive income for the three months ended March 31, 2011 | | | | | | | | 93,617 | (51) | 93,566 |
| Cash dividends ($0.14 per share) | | | | (11,995) | | | | (11,995) | | (11,995) |
| Stock-based compensation | | 4,191 | 309 | | | | | 4,500 | | 4,500 |
| Balance, March 31, 2011 | $ 44,388 | $ 590,783 | $ (25,763) | $ 2,488,447 | $ 373,506 | $ (5,749) | $ (48,403) | $ 3,417,209 | $ (1,035) | $ 3,416,174 |
| Net income for the three months ended June 30, 2011 | | | | 93,068 | | | | 93,068 | 296 | 93,364 |
| Change in net unrealized gains/losses on investments (net of income tax - $85,553) | | | | | 158,888 | | | 158,888 | | 158,888 |
| Reclassification adjustment for investment amounts included in net income (net of income tax - $(7,271)) | | | | | (13,508) | | | (13,508) | | (13,508) |
| Change in net unrealized gains/losses relating to other-than-temporary | | | | | (10,111) | | | (10,111) | | (10,111) |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| impaired investments for which a portion has been recognized in earnings (net of income tax $(5,444)) | | | | | | | | | | |
| Change in accumulated gain (loss) derivatives (net of income tax - $(1,777)) | | | | | | (3,299) | | (3,299) | | (3,299) |
| Reclassification adjustment for derivative amounts included in net income (net of income tax - $238) | | | | | | 443 | | 443 | | 443 |
| Change in postretirement benefits liability adjustment (net of income tax - $(451)) | | | | | | | (838) | (838) | | (838) |
| Comprehensive income for the three months ended June 30, 2011 | | | | | | | | 224,643 | 296 | 224,939 |
| Cash dividends ($0.16 per share) | | | | (13,719) | | | | (13,719) | | (13,719) |
| Repurchase of common stock | | | (24,893) | | | | | (24,893) | | (24,893) |
| Stock-based compensation | | 1,668 | 330 | | | | | 1,998 | | 1,998 |
| Balance, June 30, 2011 | $ 44,388 | $ 592,451 | $ (50,326) | $ 2,567,796 | $ 508,775 | $ (8,605) | $ (49,241) | $ 3,605,238 | $ (739) | $ 3,604,499 |

See Notes to Consolidated Condensed Financial Statements

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**CONSOLIDATED CONDENSED STATEMENTS OF SHAREOWNERS EQUITY**

(Unaudited)

(continued)

| | Common Stock | Additional Paid-In-Capital | Treasury Stock | Retained Earnings | Accumulated Other Comprehensive Income (Loss): Net Unrealized Gains / (Losses) on Investments | Accumulated Other Comprehensive Income (Loss): Accumulated Gain / (Loss) Derivatives | Accumulated Other Comprehensive Income (Loss): Minimum Pension Liability Adjustments | Total Protective Life Corporation s shareowners equity | Non controlling Interest | Total Equity |
|---|---|---|---|---|---|---|---|---|---|---|
| | (Dollars In Thousands) | | | | | | | | | |
| Net income for the three months ended September 30, 2011 | | | | 88,614 | | | | 88,614 | | 88,614 |
| Change in net unrealized gains/losses on investments (net of income tax - $238,985) | | | | | 443,832 | | | 443,832 | | 443,832 |
| Reclassification adjustment for investment amounts included in net income (net of income tax - $(3,814)) | | | | | (7,087) | | | (7,087) | | (7,087) |
| Change in net unrealized gains/losses relating to other-than-temporary impaired investments for which a portion has been recognized in earnings (net of income tax $(509)) | | | | | (944) | | | (944) | | (944) |
| Change in accumulated gain (loss) derivatives (net of income tax - $(420)) | | | | | | (780) | | (780) | | (780) |
| Reclassification adjustment for derivative amounts included in net income (net of income tax - $(355)) | | | | | | (659) | | (659) | | (659) |
| Change in postretirement benefits liability adjustment (net of income tax - $(451)) | | | | | | | (839) | (839) | | (839) |
| Comprehensive income for the three months ended September 30, 2011 | | | | | | | | 522,137 | | 522,137 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Cash dividends ($0.16 per share) | | | | (13,550) | | | | (13,550) | | (13,550) |
| Repurchase of common stock | | | (33,587) | | | | | (33,587) | | (33,587) |
| Stock-based compensation | | 1,633 | 364 | | | | | 1,997 | | 1,997 |
| Balance, September 30, 2011 | $ 44,388 | $ 594,084 | $ (83,549) | $ 2,642,860 | $ 944,576 | $ (10,044) | $ (50,080) | $ 4,082,235 | $ (739) | $ 4,081,496 |

See Notes to Consolidated Condensed Financial Statements

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**

(Unaudited)

| | For The Nine Months Ended September 30, 2011 | 2010 |
|---|---|---|
| | (Dollars In Thousands) | |
| **Cash flows from operating activities** | | |
| Net income | $ 249,444 | $ 181,321 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Realized investment losses (gains) | (31,145) | 46,886 |
| Amortization of deferred policy acquisition costs and value of business acquired | 237,833 | 146,761 |
| Capitalization of deferred policy acquisition costs | (361,644) | (365,499) |
| Depreciation expense | 6,777 | 7,184 |
| Deferred income tax | 30,148 | (5,813) |
| Accrued income tax | 34,440 | 112,281 |
| Interest credited to universal life and investment products | 740,328 | 658,488 |
| Policy fees assessed on universal life and investment products | (528,739) | (471,383) |
| Change in reinsurance receivables | (27,540) | (230,423) |
| Change in accrued investment income and other receivables | (31,583) | (38,996) |
| Change in policy liabilities and other policyholders funds of traditional life and health products | 7,227 | 328,042 |
| Trading securities: | | |
| Maturities and principal reductions of investments | 228,405 | 262,153 |
| Sale of investments | 655,607 | 555,904 |
| Cost of investments acquired | (736,587) | (769,120) |
| Other net change in trading securities | 31,307 | 20,078 |
| Change in other liabilities | 47,114 | 23,478 |
| Other income - surplus note repurchase | (36,962) | (13,337) |
| Other, net | (5,004) | 126,490 |
| **Net cash provided by operating activities** | 509,426 | 574,495 |
| **Cash flows from investing activities** | | |
| Maturities and principal reductions of investments, available-for-sale | 1,144,228 | 1,372,385 |
| Sale of investments, available-for-sale | 2,251,034 | 2,807,438 |
| Cost of investments acquired, available-for sale | (4,184,350) | (5,274,565) |
| Mortgage loans: | | |
| New borrowings | (408,602) | (231,931) |
| Repayments | 344,921 | 249,363 |
| Change in investment real estate, net | 521 | (1,127) |
| Change in policy loans, net | 13,806 | 27,062 |
| Change in other long-term investments, net | 36,367 | (138,419) |
| Change in short-term investments, net | 129,129 | 517,278 |
| Net unsettled security transactions | 127,621 | 80,412 |
| Purchase of property and equipment | (12,896) | (7,050) |
| Payments for business acquisitions, net of cash acquired of $35,959 | (209,609) | |
| **Net cash used in investing activities** | (767,830) | (599,154) |
| **Cash flows from financing activities** | | |
| Borrowings under line of credit arrangements and debt | 20,000 | 116,000 |
| Principal payments on line of credit arrangement and debt | (26,852) | (275,000) |
| Issuance (repayment) of non-recourse funding obligations | (117,600) | (27,000) |

| | | | | |
|---|---|---|---|---|
| Reverse repurchase borrowings | | 157,103 | | |
| Dividends to shareowners | | (39,264) | | (34,257) |
| Repurchase of common stock | | (58,480) | | |
| Investments product deposits and change in universal life deposits | | 3,413,567 | | 2,652,811 |
| Investment product withdrawals | | (2,998,684) | | (2,459,566) |
| Other financing activities, net | | (23,324) | | (2,314) |
| **Net cash provided by (used in) financing activities** | | 326,466 | | (29,326) |
| **Change in cash** | | 68,062 | | (53,985) |
| **Cash at beginning of period** | | 264,425 | | 205,325 |
| **Cash at end of period** | $ | 332,487 | $ | 151,340 |

See Notes to Consolidated Condensed Financial Statements

Table of Contents

**PROTECTIVE LIFE CORPORATION**

**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

(Unaudited)

## 1. BASIS OF PRESENTATION

### Basis of Presentation

The accompanying unaudited consolidated condensed financial statements of Protective Life Corporation and subsidiaries (the Company ) have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the disclosures required by GAAP for complete financial statements. In the opinion of management, the accompanying financial statements reflect all adjustments (consisting only of normal recurring items) necessary for a fair statement of the results for the interim periods presented. Operating results for the three and nine month periods ended September 30, 2011, are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. The year-end consolidated condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP. For further information, refer to the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010.

The operating results of companies in the insurance industry have historically been subject to significant fluctuations due to changing competition, economic conditions, interest rates, investment performance, insurance ratings, claims, persistency, and other factors.

### Reclassifications

Certain reclassifications have been made in the previously reported financial statements and accompanying notes to make the prior year amounts comparable to those of the current year. Such reclassifications had no effect on previously reported net income or shareowners equity.

### Entities Included

The consolidated condensed financial statements include the accounts of Protective Life Corporation and subsidiaries and its affiliate companies in which the Company holds a majority voting or economic interest. Intercompany balances and transactions have been eliminated.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Accounting Pronouncements Recently Adopted**

**Accounting Standard Update ( ASU or Update ) No. 2010-06 Fair Value Measurements and Disclosures Improving Disclosures about Fair Value Measurements**. In January of 2010, the Financial Accounting Standards Board ( FASB ) issued ASU No. 2010-06 Fair Value Measurements and Disclosures Improving Disclosures about Fair Value Measurements. This Update provides amendments to Subtopic 820-10 that requires the following new disclosures. 1) A reporting entity should disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. 2) In the reconciliation for fair value measurements using significant unobservable inputs (Level 3), a reporting entity should present separately information about purchases, sales, issuances, and settlements (that is, on a gross basis rather than as one net number).

This Update provides amendments to Subtopic 820-10 that clarifies existing disclosures. 1) A reporting entity should provide fair value measurement disclosures for each class of assets and liabilities. 2) A reporting entity should provide disclosures about the valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements. Those disclosures are required for fair value measurements that fall in either Level 2 or Level 3. This Update also includes conforming amendments to the guidance on employers disclosures about postretirement benefit plan assets (Subtopic 715-20). The conforming amendments to Subtopic 715-20 change the terminology from *major categories* of assets to *classes* of assets and provide a cross reference to the guidance in Subtopic 820-10 on how to determine appropriate classes to present fair value disclosures. This Update is effective for interim and annual reporting periods beginning after December 15, 2009, which the Company adopted for the period ending March 31, 2010, except for the disclosures about purchases, sales,

Table of Contents

issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures were adopted by the Company as of January 1, 2011. This Update did not have an impact on the Company s results of operations or financial position.

**ASU No. 2010-15 Financial Services Insurance How Investments Held through Separate Accounts Affect an Insurer s Consolidation Analysis of Those Investments**. The amendments in this Update clarify that an insurance entity should not consider any separate account interests held for the benefit of policy holders in an investment to be the insurer s interests. The entity should not combine general account and separate account interests in the same investment when assessing the investment for consolidation. Additionally, the amendments do not require an insurer to consolidate an investment in which a separate account holds a controlling financial interest if the investment is not or would not be consolidated in the standalone financial statements of the separate account. The amendments in this Update also provide guidance on how an insurer should consolidate an investment fund in situations in which the insurer concludes that consolidation is required. This Update is effective for fiscal years beginning after December 15, 2010. For the Company this Update became effective January 1, 2011. This Update did not have an impact on the Company s results of operations or financial position.

**ASU No. 2010-20 Receivables Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses**. The objective of this Update is to require disclosures that facilitate financial statement users in evaluating the nature of credit risk inherent in the portfolio of financing receivables (loans); how that risk is analyzed and assessed in arriving at the allowance for credit losses; and any changes and the reasons for those changes to the allowance for credit losses. The Update requires several new disclosures regarding the reserve for credit losses which was effective on December 31, 2010 and provisions related to troubled debt restructurings which became effective for fiscal periods beginning after June 30, 2011. The Company adopted the new disclosures in this Update for the annual reporting period ending December 31, 2010 and adopted the provisions related to troubled debt restructuring in the third quarter of 2011. This Update did not have an impact on the Company s results of operations or financial position.

**ASU No. 2010-28 Intangibles Goodwill and Other When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts**. The amendments in this Update modify Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity is required to perform Step 2 of the goodwill impairment test if it is more likely than not that a goodwill impairment exists. In determining whether it is more likely than not that a goodwill impairment exists, an entity should consider whether there are any adverse qualitative factors indicating that an impairment may exist. This Update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. This Update was effective for the Company as of January 1, 2011. This Update did not have an impact on the Company s results of operations or financial position.

**ASU No. 2010-29 Business Combinations Disclosure of Supplementary Pro Forma Information for Business Combinations.** This Update does not change current accounting for business combinations, however it clarifies the current guidance regarding pro forma disclosures and requires a description of the nature and amount of material, nonrecurring pro forma adjustments to arrive at pro forma revenue and earnings. The amendments in this Update were effective prospectively for business combinations for which the acquisition date is on or after January 1, 2011. The Company applied this guidance to the pro forma information related to the reinsurance transaction with Liberty Life Insurance Company as disclosed in Note 3 *Significant Acquisitions*. We will apply the guidance to all future acquisitions. There was no material impact to the adoption of this Update.

**ASU No. 2011-02 Receivables A Creditor s Determination of Whether a Restructuring Is a Troubled Debt Restructuring**. The objective of this Update is to evaluate whether a restructuring constitutes a troubled debt restructuring. In evaluating whether a restructuring constitutes a troubled debt restructuring, a creditor must separately conclude that both of the following exist: 1) the restructuring constitutes a concession and 2) the debtor is experiencing financial difficulties. This Update also clarifies the guidance on a creditor s evaluation of whether it has granted a concession. The amendments in this Update are effective for the first interim or annual period beginning on or after June 15, 2011, and should be applied retrospectively to the beginning of the annual period of adoption. For the Company, this Update became effective on July 1, 2011. This

Update did not have an impact on the Company s results of operations or financial position.

Table of Contents

**Accounting Pronouncements Not Yet Adopted**

**ASU No. 2010-26 Financial Services Insurance - Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts**. The objective of this Update is to address diversity in practice regarding the interpretation of which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral. This Update prescribes that certain incremental direct costs of successful initial or renewal contract acquisitions may be deferred. It defines incremental direct costs as those costs that result directly from and are essential to the contract transaction and would not have been incurred by the insurance entity had the contract transaction not occurred. This Update also clarifies the definition of the types of incurred costs that may be capitalized and the accounting and recognition treatment of advertising, research, and other administrative costs related to the acquisition of insurance contracts. This Update is effective for periods beginning after December 15, 2011 and is to be applied prospectively. Early adoption and retrospective application are optional. The Company s expected retrospective adoption of this Update will result in a reduction in its deferred acquisition cost asset as well as a decrease in the amortization associated with those previously deferred costs. There will also be a reduction in the level of costs the Company defers subsequent to adoption. The Company is evaluating the full effects of implementing this Update, but the Company currently estimates that its retrospective adoption will result in a cumulative effect adjustment to the opening balance of shareowners equity of between 13% and 15% as of January 1, 2012, including a reduction of between approximately 20% and 22% of its existing deferred acquisition cost asset balance as of January 1, 2012. The Company currently estimates that if the change were in effect at September 30, 2011, the adoption of this Update would have resulted in a year-to-date decrease to net income in 2011 of between 8% and 10%.

**ASU No. 2011-03 Transfers and Servicing - Reconsideration of Effective Control for Repurchase Agreements**. This Update amends the assessment of effective control for repurchase agreements to remove 1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and 2) the collateral maintenance implementation guidance related to the criterion. The Boards determined that these criterion should not be a determining factor of effective control. This Update is effective for the first interim or annual period beginning on or after December 15, 2011. For the Company, the Update will be applied to all repurchase agreements beginning January 1, 2012. The Company is currently evaluating the impact this Update will have on its results of operations or financial position.

**ASU No. 2011-04 Fair Value Measurement - Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs**. The amendments in this Update result in common fair value measurement and disclosure requirements in GAAP and International Financial Reporting Standards ( IFRSs ). The amendments change the wording used to describe many of the requirements for measuring fair value and for disclosing information about fair value measurements. The intent of this Update was not to change the application of the requirements in Topic 820. Some of the amendments clarify the intent regarding the application of existing fair value measurement requirements. The Update did modify several principles or requirements for measuring fair value or for disclosing information about fair value measurements. These changes are effective for interim and annual periods beginning after December 15, 2011. The Company is currently evaluating the impact this Update will have on its results of operations or financial position.

**ASU No. 2011-05 Comprehensive Income Presentation of Comprehensive Income**. In this Update, a company has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in 1) a single continuous statement of comprehensive income, or 2) in two separate but consecutive statements. In both choices, a company is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. The amendments in this Update do not change the items that must be reported in other comprehensive income, or the timing of its subsequent reclassification to net income. This Update is effective January 1, 2012. The Company is currently evaluating the appropriate format to which it will adhere.

**ASU No. 2011-08 Intangibles Goodwill and Other: Testing Goodwill for Impairment**. This Update is intended to reduce the complexity and cost of goodwill impairment testing by allowing an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment prior to the quantitative calculation required by current guidance. Under the amendments to Topic 350, an entity has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an entity determines it is not more likely than not that the fair value is less than the carrying amount, the two-step impairment process is not required. However, if an entity concludes otherwise, the two-step impairment test outlined in current guidance is required to be completed. This Update does not change the requirements or implementation of the current two-step impairment

Table of Contents

test. This Update is effective January 1, 2012. The Company is currently evaluating the appropriate process to which it will adhere.

**Significant Accounting Policies**

For a full description of significant accounting policies, see Note 2 of Notes to Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2010. There were no significant changes to the Company s accounting policies during the nine months ended September 30, 2011, except as noted above. See Note 5, *Mortgage Loans* for additional information on the accounting policies for mortgage loans.

## 3. SIGNIFICANT ACQUISITIONS

On December 31, 2010, Protective Life Insurance Company ( PLICO ), the Company s principal operating subsidiary, completed the acquisition of all of the outstanding stock of United Investors Life Insurance Company ( United Investors ), pursuant to a Stock Purchase Agreement, between PLICO, Torchmark Corporation ( Torchmark ) and its wholly owned subsidiaries, Liberty National Life Insurance Company ( Liberty National ) and United Investors.

The Company accounted for this transaction under the purchase method of accounting as required by FASB guidance under the ASC Business Combinations topic. This guidance requires that the total purchase price be allocated to the assets acquired and liabilities assumed based on their fair values at the acquisition date. The aggregate purchase price for United Investors was $363.3 million.

On April 29, 2011, PLICO closed a previously announced and unrelated reinsurance transaction with Liberty Life Insurance Company ( Liberty Life ) under the terms of which PLICO reinsured substantially all of the life and health business of Liberty Life. The transaction closed in conjunction with Athene Holding Ltd s acquisition of Liberty Life from an affiliate of Royal Bank of Canada. The capital invested by PLICO in the transaction at closing was $321 million, including a $225 million ceding commission. In conjunction with the closing, PLICO invested $40 million in a surplus note issued by Athene Life Re. The Company accounted for this transaction in a manner consistent with the purchase method of accounting as required by FASB guidance under the ASC Business Combinations topic. This guidance requires that the total consideration paid be allocated to the assets acquired and liabilities assumed based on their fair values at the transaction date.

The following table summarizes the fair values of the net assets acquired from the Liberty Life reinsurance transaction as of the transaction date:

| | Fair Value as of April 29, 2011 (Dollars In Thousands) |
|---|---|
| **ASSETS** | |
| Investments | $ 1,768,297 |
| Cash | 35,959 |
| Accrued investment income | 154 |

| | | |
|---|---|---|
| Accounts and premiums receivable, net | | 877 |
| Reinsurance receivable | | 9,511 |
| Value of business acquired | | 135,876 |
| Other assets | | 1 |
| Assets related to separate accounts | | |
| Total assets | | 1,950,675 |
| **LIABILITIES** | | |
| Policy liabilities and accrual | | 1,665,294 |
| Annuity account balances | | 4,420 |
| Other policyholders funds | | 24,977 |
| Other liabilities | | 30,834 |
| Total liabilities | | 1,725,525 |
| | | |
| **NET ASSETS ACQUIRED** | $ | 225,150 |

Table of Contents

The following (unaudited) pro forma condensed consolidated results of operations assumes that the aforementioned transactions with Liberty Life and United Investors were completed as of January 1, 2010:

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands) | | | |
| Revenue | $ 939,381(1) | $ 943,533 | $ 2,762,074(1) | $ 2,723,605 |
| Net income | $ 88,614(2) | $ 104,833 | $ 250,236(2) | $ 280,319 |
| EPS - basic | $ 1.05 | $ 1.21 | $ 2.91 | $ 3.24 |
| EPS - diluted | $ 1.03 | $ 1.20 | $ 2.87 | $ 3.20 |

(1) Includes $66.5 million and $111.3 million of total revenue for Liberty Life and $26.6 million and $79.4 million of total revenue for UILIC, respectively, since the transaction date for the three and nine months ended September 30, 2011.

(2) Includes $15.9 million and $25.6 million of operating income for Liberty Life and $ 3.7 million and $15.7 million of operating income for UILIC, respectively, since the transaction date for the three and nine months ended September 30, 2011.

## 4. INVESTMENT OPERATIONS

Net realized investment gains (losses) for all other investments are summarized as follows:

| | For The Three Months Ended September 30, 2011 | For The Nine Months Ended September 30, 2011 |
|---|---|---|
| | (Dollars In Thousands) | |
| Fixed maturities | $ 20,721 | $ 56,212 |
| Equity securities | 9 | 9,179 |
| Impairments on fixed maturity securities | (9,829) | (24,979) |
| Impairments on equity securities | | |
| Modco trading portfolio | 123,760 | 151,714 |
| Other investments | (6,260) | (15,486) |
| Total realized gains (losses) - investments | $ 128,401 | $ 176,640 |

For the three and nine months ended September 30, 2011, gross realized gains on investments available-for-sale (fixed maturities, equity securities, and short-term investments) were $23.2 million and $69.7 million and gross realized losses were $12.4 million and $29.0 million, including $9.8 million and $24.7 million of impairment losses, respectively. The $24.7 million excludes $0.3 million of impairment losses in the trading portfolio for the nine months ended September 30, 2011.

The $9.2 million of gains included in equity securities for the nine months ended September 30, 2011, primarily relates to gains of $6.9 million on securities that have recovered in value as the issuer exited bankruptcy and $1.2 million that relates to gains recognized on the sale of Federal National Mortgage Association preferreds.

For the three and nine months ended September 30, 2011, the Company sold securities in an unrealized gain position with a fair value (proceeds) of $350.7 million and $1.8 billion, respectively. The gain realized on the sale of these securities was $23.2 million and $69.7 million, respectively.

For the three and nine months ended September 30, 2011, the Company sold securities in an unrealized loss position with a fair value (proceeds) of $48.5 million and $211.5 million, respectively. The loss realized on the sale of these securities was $2.5 million and $4.3 million, respectively.

Table of Contents

The amortized cost and fair value of the Company s investments classified as available-for-sale as of September 30, 2011, are as follows:

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value | Total OTTI Recognized in OCI(1) |
|---|---|---|---|---|---|
| | | | (Dollars In Thousands) | | |
| Fixed maturities: | | | | | |
| Bonds | | | | | |
| Residential mortgage-backed securities | $ 2,543,463 | $ 100,445 | $ (110,718) | $ 2,533,190 | $ (43,905) |
| Commercial mortgage-backed securities | 463,075 | 9,322 | (7,960) | 464,437 | |
| Other asset-backed securities | 870,801 | 2,769 | (72,811) | 800,759 | |
| U.S. government-related securities | 1,244,622 | 92,094 | (139) | 1,336,577 | |
| Other government-related securities | 127,260 | 6,507 | (800) | 132,967 | |
| States, municipals, and political subdivisions | 1,148,313 | 176,289 | | 1,324,602 | |
| Corporate bonds | 16,743,208 | 1,793,426 | (272,437) | 18,264,197 | 1,739 |
| | 23,140,742 | 2,180,852 | (464,865) | 24,856,729 | (42,166) |
| Equity securities | 326,988 | 5,050 | (13,971) | 318,067 | (73) |
| Short-term investments | 12,744 | | | 12,744 | |
| | $ 23,480,474 | $ 2,185,902 | $ (478,836) | $ 25,187,540 | $ (42,239) |

(1) These amounts are included in the gross unrealized gains and gross unrealized losses column above.

As of September 30, 2011, the Company had an additional $3.0 billion of fixed maturities, $9.7 million of equity securities, and $67.6 million of short-term investments classified as trading securities.

The amortized cost and fair value of available-for-sale fixed maturities as of September 30, 2011, by expected maturity, are shown below. Expected maturities of securities without a single maturity date are allocated based on estimated rates of prepayment that may differ from actual rates of prepayment.

| | Amortized Cost | Fair Value |
|---|---|---|
| | (Dollars In Thousands) | |
| Due in one year or less | $ 586,074 | $ 594,660 |
| Due after one year through five years | 4,591,736 | 4,769,481 |
| Due after five years through ten years | 5,864,950 | 6,274,144 |
| Due after ten years | 12,097,982 | 13,218,444 |
| | $ 23,140,742 | $ 24,856,729 |

Each quarter the Company reviews investments with unrealized losses and tests for other-than-temporary impairments. The Company analyzes various factors to determine if any specific other-than-temporary asset impairments exist. These include, but are not limited to: 1) actions taken by rating agencies, 2) default by the issuer, 3) the significance of the decline, 4) an assessment of the Company s intent to sell the security (including a more likely than not assessment of whether the Company will be required to sell the security) before recovering the security s amortized cost, 5) the time period during which the decline has occurred, 6) an economic analysis of the issuer s industry, and 7) the financial strength, liquidity, and recoverability of the issuer. Management performs a security by security review each quarter in evaluating the need for

any other-than-temporary impairments. Although no set formula is used in this process, the investment performance, collateral position, and continued viability of the issuer are significant measures considered, and in some cases, an analysis regarding the Company s expectations for recovery of the security s entire amortized cost basis through the receipt of future cash flows is performed. Once a determination has been made that a specific other-than-temporary impairment exists, the security s basis is adjusted and an other-than-temporary impairment is recognized. Equity securities that are other-than-temporarily impaired are written down to fair value with a realized loss recognized in earnings.

Other-than-temporary impairments to debt securities that the Company does not intend to sell and does not expect to be required to sell before recovering the security s amortized cost are written down to discounted expected future cash flows ( post impairment cost ) and credit losses are recorded in earnings. The difference between the securities discounted expected future cash flows and the fair value of the securities is recognized in other comprehensive income (loss) as a non-credit portion of the recognized other-than-temporary impairment. When calculating the post impairment cost for residential mortgage-backed securities ( RMBS ), commercial mortgage-backed securities ( CMBS ), and other asset-backed securities, the Company considers all known market data related to cash flows to estimate future cash flows. When calculating the post impairment cost for corporate debt securities, the Company considers all contractual cash flows to estimate expected future cash flows. To calculate the post impairment cost, the expected future cash flows are discounted at

Table of Contents

the original purchase yield. Debt securities that the Company intends to sell or expects to be required to sell before recovery are written down to fair value with the change recognized in earnings.

During the three and nine months ended September 30, 2011, the Company recorded other-than-temporary impairments on investments of $6.2 million and $37.9 million, respectively, related to debt securities. Of the $6.2 million of impairments for the three months ended September 30, 2011, $9.8 million was recorded in earnings and $3.6 million of non-credit gains was recorded in other comprehensive income (loss). The $3.6 million of non-credit gains includes $1.3 million of losses related to newly impaired securities and a net gain of $4.9 million related to previously impaired securities that are now in a gain position. Of the $37.9 million of impairments for the nine months ended September 30, 2011, $25.0 million was recorded in earnings and $12.9 million was recorded in other comprehensive income (loss). During this period, there were no other-than-temporary impairments related to debt securities or equity securities that the Company intends to sell or expects to be required to sell, except with respect to certain debt securities that were part of the Company s collateral in its securities lending program.

For the three and nine months ended September 30, 2011, there were no other-than-temporary impairments related to equity securities.

The following chart is a rollforward of available-for-sale credit losses on debt securities held by the Company for which a portion of an other-than-temporary impairment was recognized in other comprehensive income (loss):

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands) | | | |
| Beginning balance | $ 49,847 | $ 31,576 | $ 39,427 | $ 25,076 |
| Additions for newly impaired securities | 744 | 6,211 | 10,150 | 25,661 |
| Additions for previously impaired securities | 6,647 | 1,179 | 10,750 | 2,930 |
| Reductions for previously impaired securities due to a change in expected cash flows | | | | |
| Reductions for previously impaired securities that were sold in the current period | | (2,947) | (3,089) | (17,648) |
| Other | | | | |
| Ending balance | $ 57,238 | $ 36,019 | $ 57,238 | $ 36,019 |

The following table includes the gross unrealized losses and fair value of the Company s investments that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of September 30, 2011:

| | Less Than 12 Months | | 12 Months or More | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Loss | Fair Value | Unrealized Loss | Fair Value | Unrealized Loss |
| | (Dollars In Thousands) | | | | | |
| Residential mortgage-backed securities | $ 271,390 | $ (14,120) | $ 625,419 | $ (96,598) | $ 896,809 | $ (110,718) |
| Commercial mortgage-backed securities | 155,685 | (7,960) | | | 155,685 | (7,960) |

| | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Other asset-backed securities | | 145,067 | | (8,864) | | 445,913 | | (63,947) | | 590,980 | | (72,811) |
| U.S. government-related securities | | 94,559 | | (139) | | | | | | 94,559 | | (139) |
| Other government-related securities | | 19,633 | | (800) | | | | | | 19,633 | | (800) |
| States, municipals, and political subdivisions | | | | | | | | | | | | |
| Corporate bonds | | 2,159,172 | | (146,475) | | 475,384 | | (125,962) | | 2,634,556 | | (272,437) |
| Equities | | 53,548 | | (5,607) | | 22,129 | | (8,364) | | 75,677 | | (13,971) |
| | $ | 2,899,054 | $ | (183,965) | $ | 1,568,845 | $ | (294,871) | $ | 4,467,899 | $ | (478,836) |

The RMBS have a gross unrealized loss greater than twelve months of $96.6 million as of September 30, 2011. These losses relate to a widening in spreads and defaults as a result of continued weakness in the residential housing market which have reduced the fair value of the RMBS holdings. Factors such as the credit enhancement within the deal structure, the average life of the securities, and the performance of the underlying collateral support the recoverability of these investments.

Table of Contents

The other asset-backed securities have a gross unrealized loss greater than twelve months of $63.9 million as of September 30, 2011. This category predominately includes student-loan backed auction rate securities, the underlying collateral, of which is at least 97% guaranteed by the Federal Family Education Loan Program ( FFELP ). These unrealized losses have occurred within the Company s auction rate securities ( ARS ) portfolio since the market collapse during 2008. At this time, the Company has no reason to believe that the U.S. Department of Education would not honor the FFELP guarantee, if it were necessary. In addition, the Company has the ability and intent to hold these securities until their values recover or until maturity.

The corporate bonds category has gross unrealized losses greater than twelve months of $126.0 million as of September 30, 2011. These losses relate primarily to fluctuations in credit spreads. The aggregate decline in market value of these securities was deemed temporary due to positive factors supporting the recoverability of the respective investments. Positive factors considered include credit ratings, the financial health of the issuer, the continued access of the issuer to capital markets, and other pertinent information including the Company s ability and intent to hold these securities to recovery.

The equities category has a gross unrealized loss greater than twelve months of $8.4 million as of September 30, 2011. These losses primarily relate to a widening in credit spreads on perpetual preferred stock holdings. The aggregate decline in market value of these securities was deemed temporary due to factors supporting the recoverability of the respective investments. Positive factors include credit ratings, the financial health of the issuer, the continued access of the issuer to the capital markets, and other pertinent information including the Company s ability and intent to hold these securities to recovery.

The Company does not consider these unrealized loss positions to be other-than-temporary, based on the factors discussed and because the Company has the ability and intent to hold these investments until the fair values recover, and does not intend to sell or expect to be required to sell the securities before recovering the Company s amortized cost of debt securities.

The following table includes the gross unrealized losses and fair value of the Company s investments that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2010:

| | Less Than 12 Months | | 12 Months or More | | Total | |
|---|---|---|---|---|---|---|
| | Fair Value | Unrealized Loss | Fair Value | Unrealized Loss | Fair Value | Unrealized Loss |
| | | | (Dollars In Thousands) | | | |
| Residential mortgage-backed securities | $ 237,450 | $ (17,877) | $ 1,173,541 | $ (125,334) | $ 1,410,991 | $ (143,211) |
| Commercial mortgage-backed securities | 25,679 | (933) | | | 25,679 | (933) |
| Other asset-backed securities | 167,089 | (2,452) | 594,756 | (27,212) | 761,845 | (29,664) |
| U.S. government-related securities | 144,807 | (3,071) | | | 144,807 | (3,071) |
| Other government-related securities | 33,936 | (8) | 14,993 | (7) | 48,929 | (15) |
| States, municipals, and political subdivisions | 563,352 | (22,345) | | | 563,352 | (22,345) |
| Corporate bonds | 2,264,649 | (82,343) | 835,655 | (94,843) | 3,100,304 | (177,186) |
| Equities | 11,950 | (3,321) | 13,544 | (1,961) | 25,494 | (5,282) |

| | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | $ | 3,448,912 | $ | (132,350) | $ | 2,632,489 | $ | (249,357) | $ | 6,081,401 | $ | (381,707) |

The RMBS have a gross unrealized loss greater than twelve months of $125.3 million as of December 31, 2010. These losses relate to a widening in spreads and defaults as a result of continued weakness in the residential housing market which have reduced the fair value of the RMBS holdings. Factors such as the credit enhancement within the deal structure, the average life of the securities, and the performance of the underlying collateral support the recoverability of the investments.

The other asset-backed securities have a gross unrealized loss greater than twelve months of $27.2 million as of December 31, 2010. This category predominately includes student-loan backed auction rate securities, the underlying collateral of which is at least 97% FFELP guaranteed. These losses relate to the ARS market collapse during 2008. At this time, the Company has no reason to believe that the U.S. Department of Education would not honor the FFELP guarantee, if it were necessary. In addition, the Company has the ability and intent to hold these securities until their values recover or maturity.

The corporate bonds category has gross unrealized losses greater than twelve months of $94.8 million as of December 31, 2010. These losses relate primarily to fluctuations in credit spreads. The aggregate decline in market value of these securities was deemed temporary due to positive factors supporting the recoverability of the respective investments. Positive factors considered include credit ratings, the financial health of the issuer, the

Table of Contents

continued access of the issuer to capital markets, and other pertinent information including the Company s ability and intent to hold these securities to recovery.

The Company does not consider these unrealized loss positions to be other-than-temporary, based on the factors discussed and because the Company has the ability and intent to hold these investments until the fair values recover, and does not intend to sell or expect to be required to sell the securities before recovering the Company s amortized cost of debt securities.

As of September 30, 2011, the Company had securities in its available-for-sale portfolio which were rated below investment grade of $2.3 billion and had an amortized cost of $2.5 billion. In addition, included in the Company s trading portfolio, the Company held $265.2 million of securities which were rated below investment grade. Approximately $469.3 million of the below investment grade securities were not publicly traded.

The change in unrealized gains (losses), net of income tax, on fixed maturity and equity securities, classified as available-for-sale is summarized as follows:

| | For The Three Months Ended September 30, 2011 | For The Nine Months Ended September 30, 2011 |
|---|---|---|
| | (Dollars In Thousands) | |
| Fixed maturities | $ 479,954 | $ 677,262 |
| Equity securities | (8,385) | (12,173) |

**5. MORTGAGE LOANS**

**Mortgage Loans**

The Company invests a portion of its investment portfolio in commercial mortgage loans. As of September 30, 2011, the Company s mortgage loan holdings were approximately $5.4 billion.

The Company s commercial mortgage loans are stated at unpaid principal balance, adjusted for any unamortized premium or discount, and net of valuation allowances. Interest income is accrued on the principal amount of the loan based on the loan s contractual interest rate. Amortization of premiums and discounts is recorded using the effective yield method. Interest income, amortization of premiums and discounts and prepayment fees are reported in net investment income.

As of September 30, 2011 and December 31, 2010, the Company had an allowance for mortgage loan credit losses of $9.1 million and $11.7 million, respectively. Over the past ten years, the Company s commercial mortgage loan portfolio has experienced an average credit loss factor of

approximately 0.02%. Due to such low historical losses, the Company believes that a collectively evaluated allowance would be inappropriate. The Company believes an allowance calculated through an analysis of specific loans that are believed to have a higher risk of credit impairment provides a more accurate presentation of expected losses in the portfolio and is consistent with the applicable guidance for loan impairments in ASC Subtopic 310. Since the Company uses the specific identification method for calculating reserves, it is necessary to review the economic situation of each borrower to determine those that have higher risk of credit impairment. The Company has a team of professionals that monitors borrower conditions such as payment practices, borrower credit, operating performance, and property conditions, as well as ensuring the timely payment of property taxes and insurance. Through this monitoring process, the Company assesses the risk of each loan. When issues are identified, the severity of the issues are assessed and reviewed for possible credit impairment. If a loss is probable, an expected loss calculation is performed and an allowance is established for that loan based on the expected loss. The expected loss is calculated as the excess carrying value of a loan over either the present value of expected future cash flows discounted at the loan s original effective interest rate, or the current estimated fair value of the loan s underlying collateral. A loan may be subsequently charged off at such point that the Company no longer expects to receive cash payments, the present value of future expected payments of the renegotiated loan is less than the current principal balance, or at such time that the Company is party to foreclosure or bankruptcy proceedings associated with the borrower and does not expect to recover the principal balance of the loan. A charge off is recorded by eliminating the allowance against the mortgage loan and recording the renegotiated loan or the collateral property related to the loan as investment real estate on the balance sheet, which is carried at the lower of the appraised fair value of the property or the unpaid principal balance of the loan, less estimated selling costs associated with the property.

Table of Contents

Many of the mortgage loans have call options or interest rate reset options between 3 and 10 years. However, if interest rates were to significantly increase, we may be unable to exercise the call options or increase the interest rates on our existing mortgage loans commensurate with the significantly increased market rates. Assuming the loans are called at their next call dates, approximately $69.1 million would become due in the fourth quarter of 2011, $205.2 million in 2012, $1.4 billion in 2013 through 2017, $760.3 million in 2018 through 2022, and $274.6 million thereafter.

The Company offers a type of commercial mortgage loan under which the Company will permit a loan-to-value ratio of up to 85% in exchange for a participating interest in the cash flows from the underlying real estate. As of September 30, 2011 and December 31, 2010, approximately $880.4 million and $884.7 million, respectively, of the Company s mortgage loans have this participation feature. Cash flows received as a result of this participation feature are recorded as interest income.

As of September 30, 2011, less than 0.15%, or $44.7 million, of invested assets consisted of nonperforming, restructured or are mortgage loans that were foreclosed and were converted to real estate properties. The Company does not expect these investments to adversely affect its liquidity or ability to maintain proper matching of assets and liabilities. The Company s mortgage loan portfolio consists of two categories of loans: (1) those not subject to a pooling and servicing agreement and (2) those previously a part of variable interest entity securitizations and thus subject to a contractual pooling and servicing agreement.

As of September 30, 2011, $17.2 million of mortgage loans not subject to a pooling and servicing agreement were nonperforming. None of these nonperforming loans have been restructured during the nine month period ending September 30, 2011. In addition, the Company foreclosed on some nonperforming loans and converted them to $5.0 million of real estate properties during the nine month period ending September 30, 2011.

As of September 30, 2011, $22.0 million of loans subject to a pooling and servicing agreement were nonperforming or restructured. None of these nonperforming loans have been restructured during the nine month period ending September 30, 2011. In addition, the Company foreclosed on some nonperforming loans and converted them to $0.5 million of real estate properties during the nine month period ending September 30, 2011.

The Company does not expect these investments to adversely affect its liquidity or ability to maintain proper matching of assets and liabilities.

An analysis of the change in the allowance for mortgage loan credit losses is provided in the following chart for the nine months ended September 30, 2011 and the twelve months ended December 31, 2010:

| | As of | |
|---|---|---|
| | **September 30, 2011** | **December 31, 2010** |
| | **(Dollars In Thousands)** | |
| Beginning balance | $ 11,650 | $ 1,725 |
| Charge offs | (12,750) | (1,146) |
| Recoveries | (2,386) | |
| Provision | 12,586 | 11,071 |
| Ending balance | $ 9,100 | $ 11,650 |

17

Table of Contents

It is the Company s policy to cease to carry accrued interest on loans that are over 90 days delinquent. For loans less than 90 days delinquent, interest is accrued unless it is determined that the accrued interest is not collectible. If a loan becomes over 90 days delinquent, it is the Company s general policy to initiate foreclosure proceedings unless a workout arrangement to bring the loan current is in place. For loans subject to a pooling and servicing agreement, there are certain additional restrictions and/or requirements related to workout proceedings, and as such, these loans may have different attributes and/or circumstances affecting the status of delinquency or categorization of those in nonperforming status. An analysis of the delinquent loans is shown in the following chart as of September 30, 2011:

| | 30-59 Days Delinquent | 60-89 Days Delinquent | Greater than 90 Days Delinquent | Total Delinquent |
|---|---|---|---|---|
| | | (Dollars In Thousands) | | |
| Commercial mortgage loans | $ 40,626 | $ 6,874 | $ 16,223 | $ 63,723 |
| Number of delinquent commercial mortgage loans | 6 | 3 | 9 | 18 |

The Company s commercial mortgage loan portfolio consists of mortgage loans that are collateralized by real estate. Due to the collateralized nature of the loans, any assessment of impairment and ultimate loss given a default on the loans is based upon a consideration of the estimated fair value of the real estate. The Company limits accrued interest income on impaired loans to ninety days of interest. Once accrued interest on the impaired loan is received, interest income is recognized on a cash basis. For information regarding impaired loans, please refer to the following chart as of September 30, 2011:

| | Recorded Investment | Unpaid Principal Balance | Related Allowance | Average Recorded Investment | Interest Income Recognized | Cash Basis Interest Income |
|---|---|---|---|---|---|---|
| | | | (Dollars In Thousands) | | | |
| Commercial mortgage loans: | | | | | | |
| With no related allowance recorded | $ 10,529 | $ 10,529 | $ | $ 1,504 | $ 35 | $ 101 |
| With an allowance recorded | 21,461 | 21,459 | 9,100 | 4,292 | 168 | 251 |

## 6. GOODWILL

During the nine months ended September 30, 2011, the Company decreased its goodwill balance by approximately $2.3 million. The decrease was due to adjustments in the Acquisitions segment related to tax benefits realized during 2011 on the portion of tax goodwill in excess of GAAP basis goodwill. As of September 30, 2011, the Company had an aggregate goodwill balance of $112.4 million.

Accounting for goodwill requires an estimate of the future profitability of the associated lines of business to assess the recoverability of the capitalized acquisition goodwill. The Company evaluates the carrying value of goodwill at the segment (or reporting unit) level at least annually and between annual evaluations if events occur or circumstances change that would more likely than not reduce the fair value of the reporting unit below its carrying amount. Such circumstances could include, but are not limited to: 1) a significant adverse change in legal factors or in business climate, 2) unanticipated competition, or 3) an adverse action or assessment by a regulator. When evaluating whether goodwill is impaired, the Company compares its estimate of the fair value of the reporting unit to which the goodwill is assigned to the reporting unit s carrying amount, including goodwill. The Company utilizes a fair value measurement (which includes a discounted cash flows analysis) to assess the carrying value of the reporting units in consideration of the recoverability of the goodwill balance assigned to each reporting unit as of the measurement date. The Company s material goodwill balances are attributable to certain of its operating segments (which are each considered to be reporting units). The cash flows used to determine the fair value of the Company s reporting units are dependent on a number of significant

assumptions. The Company s estimates, which consider a market participant view of fair value, are subject to change given the inherent uncertainty in predicting future results and cash flows, which are impacted by such things as policyholder behavior, competitor pricing, capital limitations, new product introductions, and specific industry and market conditions. Additionally, the discount rate used is based on the Company s judgment of the appropriate rate for each reporting unit based on the relative risk associated with the projected cash flows. As of December 31, 2010, the Company performed its annual evaluation of goodwill and determined that no adjustment to impair goodwill was necessary.

The Company also considers its market capitalization in assessing the reasonableness of the fair values estimated for its reporting units in connection with its goodwill impairment testing. In considering the Company s

Table of Contents

September 30, 2011 common equity price, which was lower than its book value per share, the Company noted there are several factors that would result in its market capitalization being lower than the fair value of its reporting units that are tested for goodwill impairment. Such factors that would not be reflected in the valuation of the Company s reporting units with goodwill include, but are not limited to: a potential concern about future earnings growth, negative market sentiment, different valuation methodologies that resulted in low valuation, and increased risk premium for holding investments in mortgage-backed securities and commercial mortgage loans. Deterioration of or adverse market conditions for certain businesses may have a significant impact on the fair value of the Company s reporting units. In the Company s view, market capitalization being below book value does not invalidate the Company s fair value assessment related to the recoverability of goodwill in its reporting units, and did not result in a triggering or impairment event.

## 7. DEBT AND OTHER OBLIGATIONS

Non-recourse funding obligations outstanding as of September 30, 2011, on a consolidated basis, are shown in the following table:

| Issuer | Balance | Maturity Year | Year-to-Date Weighted-Avg Interest Rate |
|---|---|---|---|
| | (Dollars In Thousands) | | |
| Golden Gate II Captive Insurance Company | $ 414,800 | 2052 | 1.33% |

During the nine months ended September 30, 2011, the Company repurchased $117.6 million of its outstanding non-recourse funding obligations, at a discount. These repurchases resulted in a $37.0 million pre-tax gain for the Company.

During the three months ended September 30, 2011, the Company s Medium-Term Notes of $9.9 million matured and were paid in full, along with applicable accrued interest.

Golden Gate II Captive Insurance Company ( Golden Gate II ), a special purpose financial captive insurance company wholly owned by PLICO, had $575 million of outstanding non-recourse funding obligations as of September 30, 2011. These outstanding non-recourse funding obligations were issued to special purpose trusts, which in turn issued securities to third parties. Certain of the Company s affiliates purchased a portion of these securities during 2010 and 2011. As a result of these purchases, as of September 30, 2011, securities related to $414.8 million of the outstanding balance of the non-recourse funding obligations were held by external parties and securities related to $160.2 million of the non-recourse funding obligations were held by affiliates.

Under a revolving line of credit arrangement, the Company has the ability to borrow on an unsecured basis up to an aggregate principal amount of $500 million (the Credit Facility ). The Company has the right in certain circumstances to request that the commitment under the Credit Facility be increased up to a maximum principal amount of $600 million. Balances outstanding under the Credit Facility accrue interest at a rate equal to (i) either the prime rate or the London Interbank Offered Rate ( LIBOR ), plus (ii) a spread based on the ratings of our senior unsecured long-term debt. The Credit Agreement provides that the Company is liable for the full amount of any obligations for borrowings or letters of credit, including those of PLICO, under the Credit Facility. The maturity date on the Credit Facility is April 16, 2013. There was an outstanding balance of $145.0 million at an interest rate of LIBOR plus 0.40% under the Credit Facility as of September 30, 2011.

The Company has a repurchase program, in which we may, from time to time, sell an investment security at a specific price and agree to repurchase that security at another specified price at a later date. The market value of securities to be repurchased is monitored and collateral levels are adjusted where appropriate to protect the counterparty against credit exposure. Cash received is invested in fixed maturity securities. As of September 30, 2011, the fair value of securities pledged under the repurchase program was $170.2 million and the repurchase obligation of $157.1 million was included in other liabilities in the consolidated condensed balance sheets. As of December 31, 2010, the Company did not have a balance for our repurchase program

Table of Contents

**8. COMMITMENTS AND CONTINGENCIES**

The Company has entered into indemnity agreements with each of its current directors that provide, among other things and subject to certain limitations, a contractual right to indemnification to the fullest extent permissible under the law. The Company has agreements with certain of its officers providing up to $10 million in indemnification. These obligations are in addition to the customary obligation to indemnify officers and directors contained in the Company s governance documents.

Under insurance guaranty fund laws, in most states insurance companies doing business therein can be assessed up to prescribed limits for policyholder losses incurred by insolvent companies. In addition, from time to time, companies may be asked to contribute amounts beyond prescribed limits. Most insurance guaranty fund laws provide that an assessment may be excused or deferred if it would threaten an insurer s own financial strength. The Company does not believe its insurance guaranty fund assessments will be materially different from amounts already provided for in the financial statements.

A number of civil jury verdicts have been returned against insurers, broker dealers and other providers of financial services involving sales, refund or claims practices, alleged agent misconduct, failure to properly supervise representatives, relationships with agents or persons with whom the insurer does business, and other matters. Often these lawsuits have resulted in the award of substantial judgments that are disproportionate to the actual damages, including material amounts of punitive and non-economic compensatory damages. In some states, juries, judges, and arbitrators have substantial discretion in awarding punitive non-economic compensatory damages which creates the potential for unpredictable material adverse judgments or awards in any given lawsuit or arbitration. Arbitration awards are subject to very limited appellate review. In addition, in some class action and other lawsuits, companies have made material settlement payments. Publicly held companies in general and the financial services and insurance industries in particular are also sometimes the target of law enforcement and regulatory investigations relating to the numerous laws and regulations that govern such companies. Some companies have been the subject of law enforcement or regulatory actions or other actions resulting from such investigations. The Company, in the ordinary course of business, is involved in such matters.

The Company establishes liabilities for litigation and regulatory actions when it is probable that a loss has been incurred and the amount of the loss can be reasonably estimated.  For matters where a loss is believed to be reasonably possible, but not probable, no liability is established. For such matters, the Company may provide an estimate of the possible loss or range of loss or a statement that such an estimate cannot be made.  The Company reviews relevant information with respect to litigation and regulatory matters on a quarterly and annual basis and updates its established liabilities, disclosures and estimates of reasonably possible losses or range of loss based on such reviews.

Although the Company cannot predict the outcome of any litigation or regulatory action, the Company does not believe that any such outcome will have an impact, either individually or in the aggregate, on its financial condition or results of operations that differs materially from the Company s established liabilities. Given the inherent difficulty in predicting the outcome of such matters, however, it is possible that an adverse outcome in certain such matters could be material to the Company s financial condition or results of operations for any particular reporting period.

Table of Contents

**9. COMPREHENSIVE INCOME (LOSS)**

The following table sets forth the Company s comprehensive income (loss) for the periods presented below:

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands) | | | |
| Net income | $ 88,614 | $ 70,371 | $ 249,444 | $ 181,321 |
| Change in net unrealized gains on investments, net of income tax: (three months: 2011 - $238,985; 2010 - $211,169; nine months: 2011 - $342,445; 2010 - $484,424) | 443,832 | 392,180 | 635,983 | 898,995 |
| Change in net unrealized gains (losses) relating to other-than-temporary impaired investments for which a portion has been recognized in earnings, net of income tax: (three months: 2011 - $(509); 2010 - $19,461; nine months: 2011 - $(9,561); 2010 - $9,006) | (944) | 36,141 | (17,755) | 16,725 |
| Change in accumulated (loss) gain - derivatives, net of income tax: (three months: 2011 - $(420); 2010 - $1,951; nine months: 2011 - $1,424; 2010 - $2,145) | (780) | 3,581 | 2,645 | 3,347 |
| Change in postretirement benefits liability adjustment, net of income tax: (three months: 2011 - $(451); 2010 - $325; nine months: 2011 - $(1,354); 2010 - $974) | (839) | 603 | (2,515) | 1,808 |
| Reclassification adjustment for investment amounts included in net income, net of income tax: (three months: 2011 - $(3,814); 2010 - $(3,583); nine months: 2011 - $(14,139); 2010 - $2,036) | (7,087) | (6,663) | (26,273) | 3,996 |
| Reclassification adjustment for derivative amounts included in net income, net of income tax: (three months: 2011 - $(355); 2010 - $(760); nine months: 2011 - $(478); 2010 - $(966)) | (659) | (1,368) | (887) | (1,738) |
| Comprehensive income | 522,137 | 494,845 | 840,642 | 1,104,454 |
| Comprehensive income (loss) attributable to noncontrolling interests | | 77 | (245) | 277 |
| Comprehensive income attributable to Protective Life Corporation | $ 522,137 | $ 494,922 | $ 840,397 | $ 1,104,731 |

**10. STOCK-BASED COMPENSATION**

During the nine months ended September 30, 2011, 191,000 performance shares with an estimated fair value of $5.4 million were issued. The criteria for payment of the 2011 performance awards is based primarily on the Company s average operating return on average equity ( ROE ) over a three-year period. If the Company s ROE is below 9.0%, no award is earned. If the Company s ROE is at or above 10.0%, the award maximum is earned. Awards are paid in shares of the Company s common stock. No performance share awards were issued during the nine months ended September 30, 2010.

Additionally, the Company issued 172,000 restricted stock units for the nine months ended September 30, 2011. These awards had a total fair value at grant date of $4.9 million. Approximately half of these restricted stock units vest in 2014, and the remainder vest in 2015.

Stock appreciation right ( SARs ) have been granted to certain officers of the Company to provide long-term incentive compensation based solely on the performance of the Company s common stock. The SARs are exercisable either five years after the date of grant or in three or four equal annual installments beginning one year after the date of grant (earlier upon the death, disability, or retirement of the officer, or in certain circumstances, of a change in control of the Company) and expire after ten years or upon termination of employment. The SARs activity as well as weighted-average base price is as follows:

| | | Weighted-Average Base Price per share | No. of SARs |
|---|---|---|---|
| Balance as of December 31, 2010 | $ | 21.97 | 2,324,837 |
| SARs granted | | | |
| SARs exercised / forfeited / expired | | 8.22 | 46,875 |
| Balance as of September 30, 2011 | $ | 22.25 | 2,277,962 |

There were no SARs issued for the nine months ended September 30, 2011. The Company will pay an amount in stock equal to the difference between the specified base price of the Company s common stock and the market value at the exercise date for each SAR.

Table of Contents

## 11. EMPLOYEE BENEFIT PLANS

Components of the net periodic benefit cost of the Company s defined benefit pension plan and unfunded excess benefit plan are as follows:

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands) | | | |
| Service cost benefits earned during the period | $ 2,194 | $ 2,068 | $ 6,582 | $ 6,204 |
| Interest cost on projected benefit obligation | 2,508 | 2,357 | 7,524 | 7,071 |
| Expected return on plan assets | (2,512) | (2,312) | (7,536) | (6,936) |
| Amortization of prior service cost | (98) | (98) | (294) | (294) |
| Amortization of actuarial losses | 1,388 | 1,026 | 4,164 | 3,078 |
| Total benefit cost | $ 3,480 | $ 3,041 | $ 10,440 | $ 9,123 |

During the nine months ended September 30, 2011, the Company contributed $5.7 million to its defined benefit pension plan for the 2010 plan year and $4.5 million for the 2011 plan year. In addition, during October of 2011, the Company contributed $2.2 million to the defined benefit pension plan for the 2011 plan year. The Company will continue to make contributions in future periods as necessary to at least satisfy minimum funding requirements. The Company may also make additional contributions in future periods to maintain an adjusted funding target attainment percentage ( AFTAP ) of at least 80%.

In addition to pension benefits, the Company provides life insurance benefits to eligible retirees and limited healthcare benefits to eligible retirees who are not yet eligible for Medicare. For a closed group of retirees over age 65, the Company provides a prescription drug benefit. The cost of these plans for the nine months ended September 30, 2011, was immaterial to the Company s financial statements.

## 12. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income available to PLC s common shareowners by the weighted-average number of common shares outstanding during the period, including shares issuable under various deferred compensation plans. Diluted earnings per share is computed by dividing net income available to PLC s common shareowners by the weighted-average number of common shares and dilutive potential common shares outstanding during the period, assuming the shares were not anti-dilutive, including shares issuable under various stock-based compensation plans and stock purchase contracts.

Table of Contents

A reconciliation of the numerators and denominators of the basic and diluted earnings per share is presented below:

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands, Except Per Share Amounts) | | | |
| **Calculation of basic earnings per share:** | | | | |
| Net income available to PLC s common shareowners | $ 88,614 | $ 70,448 | $ 249,199 | $ 181,598 |
| | | | | |
| Average shares issued and outstanding | 83,844,567 | 85,662,988 | 84,979,539 | 85,628,404 |
| Issuable under various deferred compensation plans | 877,665 | 940,581 | 904,130 | 927,357 |
| Weighted shares outstanding - basic | 84,722,232 | 86,603,569 | 85,883,669 | 86,555,761 |
| | | | | |
| Per share: | | | | |
| Net income available to PLC s common shareowners - basic | $ 1.05 | $ 0.81 | $ 2.90 | $ 2.10 |
| | | | | |
| **Calculation of diluted earnings per share:** | | | | |
| Net income available to PLC s common shareowners | $ 88,614 | $ 70,448 | $ 249,199 | $ 181,598 |
| | | | | |
| Weighted shares outstanding - basic | 84,722,232 | 86,603,569 | 85,883,669 | 86,555,761 |
| Stock appreciation rights ( SARs )(1) | 438,172 | 468,886 | 477,383 | 466,511 |
| Issuable under various other stock-based compensation plans | 114,881 | 110,102 | 117,453 | 134,299 |
| Restricted stock units | 729,286 | 519,035 | 674,307 | 483,650 |
| Weighted shares outstanding - diluted | 86,004,571 | 87,701,592 | 87,152,812 | 87,640,221 |
| | | | | |
| Per share: | | | | |
| Net income available to PLC s common shareowners - diluted | $ 1.03 | $ 0.80 | $ 2.86 | $ 2.07 |

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(1) Excludes 1,434,180 and 1,475,645 SARs as of September 30, 2011 and 2010, respectively, that are antidilutive. In the event the average market price exceeds the issue price of the SARs, such rights would be dilutive to the Company s earnings per share and will be included in the Company s calculation of the diluted average shares outstanding for applicable periods.

## 13. INCOME TAXES

There have been no material changes to the balance of unrecognized income tax benefits which impacted earnings for the nine months ended September 30, 2011. Within the next twelve months, the Company does not expect to have any material adjustments to its unrecognized income tax benefits liability with regard to any of the tax jurisdictions in which it conducts its business operations.

The Company has computed its effective income tax rate for the three and nine months ended September 30, 2011 and 2010, based upon its estimate of its annual 2011 and 2010 income. The effective tax rate for the three and nine months ended September 30, 2011 was 32.5% and 34.1%, respectively, and 34.2% and 33.5% for the three and nine months ended September 30, 2010, respectively.

Based on the Company s current assessment of future taxable income, including available tax planning opportunities, the Company anticipates that it is more likely than not that it will generate sufficient taxable income to realize all of its material deferred tax assets. The Company did not record a valuation allowance against its material deferred tax assets as of September 30, 2011.

**14. FAIR VALUE OF FINANCIAL INSTRUMENTS**

The Company determined the fair value of its financial instruments based on the fair value hierarchy established in FASB guidance referenced in the Fair Value Measurements and Disclosures Topic which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The Company has adopted the provisions from the FASB guidance that is referenced in the Fair Value Measurements and Disclosures Topic for non-financial assets and liabilities (such as property and equipment, goodwill, and other intangible assets) that are required to be measured at fair value on a periodic basis. The effect on the Company s periodic fair value measurements for non-financial assets and liabilities was not material.

The Company has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into a three level hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the

Table of Contents

inputs used to measure fair value fall within different levels of the hierarchy, the category level is based on the lowest priority level input that is significant to the fair value measurement of the instrument.

Financial assets and liabilities recorded at fair value on the consolidated condensed balance sheets are categorized as follows:

- **Level 1:** Unadjusted quoted prices for identical assets or liabilities in an active market.

- **Level 2:** Quoted prices in markets that are not active or significant inputs that are observable either directly or indirectly. Level 2 inputs include the following:

a) Quoted prices for similar assets or liabilities in active markets

b) Quoted prices for identical or similar assets or liabilities in non-active markets

c) Inputs other than quoted market prices that are observable

d) Inputs that are derived principally from or corroborated by observable market data through correlation or other means.

- **Level 3:** Prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. They reflect management s own assumptions about the assumptions a market participant would use in pricing the asset or liability.

Table of Contents

The following table presents the Company s hierarchy for its assets and liabilities measured at fair value on a recurring basis as of September 30, 2011:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | | (Dollars In Thousands) | | |
| **Assets:** | | | | |
| Fixed maturity securities - available-for-sale | | | | |
| Residential mortgage-backed securities | $ | $ 2,533,183 | $ 7 | $ 2,533,190 |
| Commercial mortgage-backed securities | | 455,003 | 9,434 | 464,437 |
| Other asset-backed securities | | 201,918 | 598,841 | 800,759 |
| U.S. government-related securities | 873,752 | 447,825 | 15,000 | 1,336,577 |
| States, municipals, and political subdivisions | | 1,324,529 | 73 | 1,324,602 |
| Other government-related securities | 15,011 | 117,956 | | 132,967 |
| Corporate bonds | 200 | 18,143,359 | 120,638 | 18,264,197 |
| Total fixed maturity securities - available-for-sale | 888,963 | 23,223,773 | 743,993 | 24,856,729 |
| | | | | |
| Fixed maturity securities - trading | | | | |
| Residential mortgage-backed securities | | 359,700 | | 359,700 |
| Commercial mortgage-backed securities | | 180,820 | | 180,820 |
| Other asset-backed securities | | 24,815 | 26,263 | 51,078 |
| U.S. government-related securities | 469,399 | 10,512 | 3,450 | 483,361 |
| States, municipals, and political subdivisions | | 230,812 | | 230,812 |
| Other government-related securities | | 78,644 | | 78,644 |
| Corporate bonds | | 1,572,634 | 41,226 | 1,613,860 |
| Total fixed maturity securities - trading | 469,399 | 2,457,937 | 70,939 | 2,998,275 |
| Total fixed maturity securities | 1,358,362 | 25,681,710 | 814,932 | 27,855,004 |
| Equity securities | 235,772 | 11,553 | 80,477 | 327,802 |
| Other long-term investments (1) | 91,843 | 8,696 | 8,487 | 109,026 |
| Short-term investments | 80,387 | | | 80,387 |
| Total investments | 1,766,364 | 25,701,959 | 903,896 | 28,372,219 |
| Cash | 332,487 | | | 332,487 |
| Other assets | 6,404 | | | 6,404 |
| Assets related to separate accounts | | | | |
| Variable annuity | 5,947,391 | | | 5,947,391 |
| Variable universal life | 470,283 | | | 470,283 |
| Total assets measured at fair value on a recurring basis | $ 8,522,929 | $ 25,701,959 | $ 903,896 | $ 35,128,784 |
| | | | | |
| **Liabilities:** | | | | |
| Annuity account balances (2) | $ | $ | $ 139,145 | $ 139,145 |
| Other liabilities (1) | 50,773 | 17,959 | 449,984 | 518,716 |
| Total liabilities measured at fair value on a recurring basis | $ 50,773 | $ 17,959 | $ 589,129 | $ 657,861 |

(1) Includes certain freestanding and embedded derivatives.

(2) Represents liabilities related to equity indexed annuities.

Table of Contents

The following table presents the Company s hierarchy for its assets and liabilities measured at fair value on a recurring basis as of December 31, 2010:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| | | (Dollars In Thousands) | | |
| **Assets:** | | | | |
| Fixed maturity securities - available-for-sale | | | | |
| Residential mortgage-backed securities | $ | $ 2,547,730 | $ 20 | $ 2,547,750 |
| Commercial mortgage-backed securities | | 155,125 | 19,901 | 175,026 |
| Other asset-backed securities | | 207,638 | 641,129 | 848,767 |
| U.S. government-related securities | 1,054,375 | 104,419 | 15,109 | 1,173,903 |
| States, municipals, and political subdivisions | | 963,225 | 78 | 963,303 |
| Other government-related securities | 14,993 | 186,214 | | 201,207 |
| Corporate bonds | 100 | 15,725,900 | 65,032 | 15,791,032 |
| Total fixed maturity securities - available-for-sale | 1,069,468 | 19,890,251 | 741,269 | 21,700,988 |
| | | | | |
| Fixed maturity securities - trading | | | | |
| Residential mortgage-backed securities | | 432,015 | | 432,015 |
| Commercial mortgage-backed securities | | 137,606 | | 137,606 |
| Other asset-backed securities | | 18,415 | 59,925 | 78,340 |
| U.S. government-related securities | 383,423 | 11,369 | 3,442 | 398,234 |
| States, municipals, and political subdivisions | | 160,539 | | 160,539 |
| Other government-related securities | | 126,553 | | 126,553 |
| Corporate bonds | | 1,642,664 | | 1,642,664 |
| Total fixed maturity securities - trading | 383,423 | 2,529,161 | 63,367 | 2,975,951 |
| Total fixed maturity securities | 1,452,891 | 22,419,412 | 804,636 | 24,676,939 |
| Equity securities | 271,483 | 10,831 | 77,098 | 359,412 |
| Other long-term investments (1) | 6,794 | 3,808 | 25,065 | 35,667 |
| Short-term investments | 344,796 | 8,028 | | 352,824 |
| Total investments | 2,075,964 | 22,442,079 | 906,799 | 25,424,842 |
| Cash | 264,425 | | | 264,425 |
| Other assets | 6,222 | | | 6,222 |
| Assets related to separate accounts | | | | |
| Variable annuity | 5,170,193 | | | 5,170,193 |
| Variable universal life | 534,219 | | | 534,219 |
| Total assets measured at fair value on a recurring basis | $ 8,051,023 | $ 22,442,079 | $ 906,799 | $ 31,399,901 |
| | | | | |
| **Liabilities:** | | | | |
| Annuity account balances (2) | $ | $ | $ 143,264 | $ 143,264 |
| Other liabilities (1) | 23,995 | 28,987 | 190,529 | 243,511 |
| Total liabilities measured at fair value on a recurring basis | $ 23,995 | $ 28,987 | $ 333,793 | $ 386,775 |

(1) Includes certain freestanding and embedded derivatives.

(2) Represents liabilities related to equity indexed annuities.

**Determination of fair values**

The valuation methodologies used to determine the fair values of assets and liabilities reflect market participant assumptions and are based on the application of the fair value hierarchy that prioritizes observable market inputs over unobservable inputs. The Company determines the fair values of certain financial assets and financial liabilities based on quoted market prices, where available. The Company also determines certain fair values based on future cash flows discounted at the appropriate current market rate. Fair values reflect adjustments for counterparty credit quality, the Company s credit standing, liquidity, and where appropriate, risk margins on unobservable parameters. The following is a discussion of the methodologies used to determine fair values for the financial instruments as listed in the above table.

Table of Contents

The fair value of fixed maturity, short-term, and equity securities is determined by management after considering one of three primary sources of information: third party pricing services, non-binding independent broker quotations, or pricing matrices. Security pricing is applied using a waterfall approach whereby publicly available prices are first sought from third party pricing services, the remaining unpriced securities are submitted to independent brokers for non-binding prices, or lastly, securities are priced using a pricing matrix. Typical inputs used by these three pricing methods include, but are not limited to: benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data including market research publications. Third party pricing services price over 90% of the Company s fixed maturity securities. Based on the typical trading volumes and the lack of quoted market prices for fixed maturities, third party pricing services derive the majority of security prices from observable market inputs such as recent reported trades for identical or similar securities making adjustments through the reporting date based upon available market observable information outlined above. If there are no recent reported trades, the third party pricing services and brokers may use matrix or model processes to develop a security price where future cash flow expectations are developed based upon collateral performance and discounted at an estimated market rate. Certain securities are priced via independent non-binding broker quotations, which are considered to have no significant unobservable inputs. When using non-binding independent broker quotations, the Company obtains one quote per security, typically from the broker from which we purchased the security. A pricing matrix is used to price securities for which the Company is unable to obtain or effectively rely on either a price from a third party pricing service or an independent broker quotation.

The pricing matrix used by the Company begins with current spread levels to determine the market price for the security. The credit spreads, assigned by brokers, incorporate the issuer s credit rating, liquidity discounts, weighted-average of contracted cash flows, risk premium, if warranted, due to the issuer s industry, and the security s time to maturity. The Company uses credit ratings provided by nationally recognized rating agencies.

For securities that are priced via non-binding independent broker quotations, the Company assesses whether prices received from independent brokers represent a reasonable estimate of fair value through an analysis using internal and external cash flow models developed based on spreads and, when available, market indices. The Company uses a market-based cash flow analysis to validate the reasonableness of prices received from independent brokers. These analytics, which are updated daily, incorporate various metrics (yield curves, credit spreads, prepayment rates, etc.) to determine the valuation of such holdings. As a result of this analysis, if the Company determines there is a more appropriate fair value based upon the analytics, the price received from the independent broker is adjusted accordingly. The Company did not adjust any quotes or prices received from brokers during the nine months ended September 30, 2011.

The Company has analyzed the third party pricing services valuation methodologies and related inputs and has also evaluated the various types of securities in its investment portfolio to determine an appropriate fair value hierarchy level based upon trading activity and the observability of market inputs that is in accordance with the Fair Value Measurements and Disclosures Topic of the ASC. Based on this evaluation and investment class analysis, each price was classified into Level 1, 2, or 3. Most prices provided by third party pricing services are classified into Level 2 because the significant inputs used in pricing the securities are market observable and the observable inputs are corroborated by the Company. Since the matrix pricing of certain debt securities includes significant non-observable inputs, they are classified as Level 3.

***Asset-Backed Securities***

This category mainly consists of residential mortgage-backed securities, commercial mortgage-backed securities, and other asset-backed securities (collectively referred to as asset-backed securities or ABS ). As of September 30, 2011, the Company held $3.8 billion of ABS classified as Level 2. These securities are priced from information provided by a third party pricing service and independent broker quotes. The third party pricing services and brokers mainly value securities using both a market and income approach to valuation. As part of this valuation process they consider the following characteristics of the item being measured to be relevant inputs: 1) weighted-average coupon rate, 2) weighted-average years to maturity, 3) types of underlying assets, 4) weighted-average coupon rate of the underlying assets, 5)

weighted-average years to maturity of the underlying assets, 6) seniority level of the tranches owned, and 7) credit ratings of the securities.

After reviewing these characteristics of the ABS, the third party pricing service and brokers use certain inputs to determine the value of the security. For ABS classified as Level 2, the valuation would consist of predominantly market observable inputs such as, but not limited to: 1) monthly principal and interest payments on

Table of Contents

the underlying assets, 2) average life of the security, 3) prepayment speeds, 4) credit spreads, 5) treasury and swap yield curves, and 6) discount margin.

As of September 30, 2011, the Company held $634.5 million of Level 3 ABS, which included $26.3 million of other asset-backed securities classified as trading. These securities are predominantly ARS whose underlying collateral is at least 97% guaranteed by the FFELP. As a result of the ARS market collapse during 2008, the Company prices its ARS using an income approach valuation model. As part of the valuation process the Company reviews the following characteristics of the ARS in determining the relevant inputs: 1) weighted-average coupon rate, 2) weighted-average years to maturity, 3) types of underlying assets, 4) weighted-average coupon rate of the underlying assets, 5) weighted-average years to maturity of the underlying assets, 6) seniority level of the tranches owned, and 7) credit ratings of the securities.

The fair value calculation of available-for-sale ABSs classified as Level 3 had, but were not limited to, the following inputs:

| | |
|---|---|
| Investment grade credit rating | 100.0% |
| Weighted-average yield | 1.5% |
| Par value | $693.7 million |
| Weighted-average life | 12.0 years |

***Corporate bonds, U.S. Government-related securities, States, municipals, and political subdivisions, and Other government related securities***

As of September 30, 2011, the Company classified approximately $21.9 billion of corporate bonds, U.S. government-related securities, states, municipals, and political subdivisions, and other government-related securities as Level 2. The fair value of the Level 2 bonds and securities is predominantly priced by broker quotes and a third party pricing service. The Company has reviewed the valuation techniques of the brokers and third party pricing service and has determined that such techniques used Level 2 market observable inputs. The following characteristics of the bonds and securities are considered to be the primary relevant inputs to the valuation: 1) weighted-average coupon rate, 2) weighted-average years to maturity, 3) seniority, and 4) credit ratings.

The brokers and third party pricing service utilize a valuation model that consists of a hybrid income and market approach to valuation. The pricing model utilizes the following inputs: 1) principal and interest payments, 2) treasury yield curve, 3) credit spreads from new issue and secondary trading markets, 4) dealer quotes with adjustments for issues with early redemption features, 5) liquidity premiums present on private placements, and 6) discount margins from dealers in the new issue market.

As of September 30, 2011, the Company classified approximately $180.4 million of bonds and securities as Level 3 valuations. The fair value of the Level 3 bonds and securities are derived from an internal pricing model that utilizes a hybrid market/income approach to valuation. The Company reviews the following characteristics of the bonds and securities to determine the relevant inputs to use in the pricing model: 1) coupon rate, 2) years to maturity, 3) seniority, 4) embedded options, 5) trading volume, and 6) credit ratings.

Level 3 bonds and securities primarily represent investments in illiquid bonds for which no price is readily available. To determine a price, the Company uses a discounted cash flow model with both observable and unobservable inputs. These inputs are entered into an industry standard

pricing model to determine the final price of the security. These inputs include: 1) principal and interest payments, 2) coupon rate, 3) sector and issuer level spreads, 4) underlying collateral, 5) credit ratings, 6) maturity, 7) embedded options, 8) recent new issuance, 9) comparative bond analysis, and 10) an illiquidity premium.

The fair value calculation of bonds and securities classified as Level 3 had, but were not limited to, the following weighted-average inputs:

| | |
|---|---|
| Investment grade credit rating | 69.8% |
| Weighted-average yield | 4.4% |
| Weighted-average coupon | 4.6% |
| Par value | $193.4 million |
| Weighted-average stated maturity | 5.7 years |

Table of Contents

***Equities***

As of September 30, 2011, the Company held approximately $92.0 million of equity securities classified as Level 2 and Level 3. Of this total, $64.6 million represents Federal Home Loan Bank ( FHLB ) stock. The Company believes that the cost of the FHLB stock approximates fair value. The remainder of these equity securities is primarily made up of holdings we have obtained through bankruptcy proceedings or debt restructurings.

***Other long-term investments and Other liabilities***

Other long-term investments and other liabilities consist entirely of free standing and embedded derivative instruments. Refer to Note 15, *Derivative Financial Instruments* for additional information related to derivatives. Derivative instruments are valued using exchange prices, independent broker quotations, or pricing valuation models, which utilize market data inputs. Excluding embedded derivatives, as of September 30, 2011, 95.9% of derivatives based upon notional values were priced using exchange prices or independent broker quotations. The remaining derivatives were priced by pricing valuation models, which predominantly utilize observable market data inputs. Inputs used to value derivatives include, but are not limited to, interest swap rates, credit spreads, interest and equity volatility, equity index levels, and treasury rates. The Company performs monthly analysis on derivative valuations that includes both quantitative and qualitative analyses.

Derivative instruments classified as Level 1 include futures, credit default swaps, and certain options, which are traded on active exchange markets.

Derivative instruments classified as Level 2 primarily include interest rate, inflation, and currency exchange swaps. These derivative valuations are determined using independent broker quotations, which are corroborated with observable market inputs.

Derivative instruments classified as Level 3 were embedded derivatives and include at least one non-observable significant input. A derivative instrument containing Level 1 and Level 2 inputs will be classified as a Level 3 financial instrument in its entirety if it has at least one significant Level 3 input.

The Company utilizes derivative instruments to manage the risk associated with certain assets and liabilities. However, the derivative instruments may not be classified within the same fair value hierarchy level as the associated assets and liabilities. Therefore, the changes in fair value on derivatives reported in Level 3 may not reflect the offsetting impact of the changes in fair value of the associated assets and liabilities.

The guaranteed minimum withdrawal benefits ( GMWB ) embedded derivative is carried at fair value in other assets and other liabilities on the Company s consolidated condensed balance sheet. The changes in fair value are recorded in earnings as Realized investment gains (losses) derivative financial instruments ; refer to Note 15, *Derivative Financial Instruments* for more information related to GMWB embedded derivative gains and losses. The fair value of the GMWB embedded derivative is derived through the income method of valuation using a valuation model that projects future cash flows using multiple risk neutral stochastic equity scenarios and policyholder behavior assumptions. The risk neutral scenarios are generated using the current swap curve and projected equity volatilities and correlations. The

projected equity volatilities are based on a blend of historical volatility and near-term equity market implied volatilities. The equity correlations are based on historical price observations. For policyholder behavior assumptions, expected lapse and utilization assumptions are used and updated for actual experience, as necessary. The Company assumes mortality of 65% of the National Association of Insurance Commissioners 1994 Variable Annuity GMDB Mortality Table. The present value of the cash flows is found using the discount rate curve, which is London Interbank Offered Rate ( LIBOR ) plus a credit spread (to represent the Company s non-performance risk). As a result of using significant unobservable inputs, the GMWB embedded derivative is categorized as Level 3. These assumptions are reviewed on a quarterly basis.

The Company has ceded certain blocks of policies under modified coinsurance agreements in which the investment results of the underlying portfolios are passed directly to the reinsurers. As a result, these agreements are deemed to contain embedded derivatives that must be reported at fair value. Changes in fair value of the embedded derivatives are reported in earnings. The investments supporting these agreements are designated as trading securities ; therefore changes in fair value of such investments are reported in earnings. The fair value of the embedded derivatives represents the unrealized gain or loss on the block of business in relation to the unrealized gain or loss of the trading securities. As a result, changes in fair value of the embedded derivatives reported in earnings are largely offset by the changes in fair value of the investments.

Table of Contents

***Annuity account balances***

The equity indexed annuity ( EIA ) model calculates the present value of future benefit cash flows less the projected future profits to quantify the net liability that is held as a reserve. This calculation is done using multiple risk neutral stochastic equity scenarios. The cash flows are discounted using LIBOR plus a credit spread. Best estimate assumptions are used for partial withdrawals, lapses, expenses and asset earned rate with a risk margin applied to each. These assumptions are reviewed annually as a part of the formal unlocking process. If an event were to occur within a quarter that would make the assumptions unreasonable, the assumptions would be reviewed within the quarter.

Included in the chart below are current key assumptions which include risk margins for the Company.

| | |
|---|---|
| Asset Earned Rate | 5.89% |
| Admin Expense per Policy | $78 to $93 per policy |
| Partial Withdrawal Rate (for ages less than 70) | 2.00% |
| Partial Withdrawal Rate (for ages 70 and greater) | 2.00% |
| Mortality | 65% of 94 GMDB table |
| Lapse | 2.2% to 55% depending on the surrender charge period |
| Return on Assets | 1.5% to 1.85% depending on the guarantee period |

The discount rate for the equity indexed annuities is based on an upward sloping rate curve which is updated each quarter. The discount rates for September 30, 2011, ranged from a one month rate of 1.86%, a 5 year rate of 3.65%, and a 30 year rate of 5.15%.

***Separate Accounts***

Separate account assets are invested in open-ended mutual funds and are included in Level 1.

Table of Contents

The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the three months ended September 30, 2011, for which the Company has used significant unobservable inputs (Level 3):

| | | Total Realized and Unrealized Gains | | Total Realized and Unrealized Losses | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Beginning Balance | Included in Earnings | Included in Other Comprehensive Income | Included in Earnings | Included in Other Comprehensive Income | Purchases | Sales | Issuances | Settlements | Transfers in/out of Level 3 | Other | Ending Balance | Total Gains (losses) included in Earnings related to Instruments still held at the Reporting Date |
| | (Dollars In Thousands) | | | | | | | | | | | | |
| **Assets:** | | | | | | | | | | | | | |
| Fixed maturity securities available-for-sale | | | | | | | | | | | | | |
| Residential mortgage-backed securities | $ 7 | $ | $ | $ | $ | $ | $ | $ | $ | $ | $ | $ 7 | $ |
| Commercial mortgage-backed securities | | | | | | | | | | 9,434 | | 9,434 | |
| Other asset-backed securities | 637,746 | | 1,478 | | (40,295) | | | | | | (88) | 598,841 | |
| U.S. government-related securities | 15,000 | | | | (3) | | | | | | 3 | 15,000 | |
| States, municipals, and political subdivisions | 74 | | | | | | (1) | | | | | 73 | |
| Other government-related securities | | | | | | | | | | | | | |
| Corporate bonds | 118,025 | | 3,388 | | (100) | | (675) | | | | | 120,638 | |
| Total fixed maturity securities - available-for-sale | 770,852 | | 4,866 | | (40,398) | | (676) | | | 9,434 | (85) | 743,993 | |
| Fixed maturity securities - trading | | | | | | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | | | | | | | |
| Commercial mortgage-backed securities | | | | | | | | | | | | | |
| Other asset-backed securities | 41,093 | 28 | | (918) | | | (14,590) | | | | 650 | 26,263 | (734) |
| U.S. government-related securities | 3,512 | | | (60) | | | | | | | (2) | 3,450 | (60) |
| States, municipals and political subdivisions | | | | | | | | | | | | | |

| | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Other government-related securities | | | | | | | | | | | | | |
| Corporate bonds | 42,041 | | | (825) | | | (71) | | | | 81 | 41,226 | (825) |
| Total fixed maturity securities - trading | 86,646 | 28 | | (1,803) | | | (14,661) | | | | 729 | 70,939 | (1,619) |
| Total fixed maturity securities | 857,498 | 28 | 4,866 | (1,803) | (40,398) | | (15,337) | | | 9,434 | 644 | 814,932 | (1,619) |
| Equity securities | 80,782 | | | | (305) | | | | | | | 80,477 | |
| Other long-term investments (1) | 27,531 | | | (19,044) | | | | | | | | 8,487 | (19,043) |
| Short-term investments | | | | | | | | | | | | | |
| Total investments | 965,811 | 28 | 4,866 | (20,847) | (40,703) | | (15,337) | | | 9,434 | 644 | 903,896 | (20,662) |
| Total assets measured at fair value on a recurring basis | $ 965,811 | $ 28 | $ 4,866 | $ (20,847) | $ (40,703) | $ | $ (15,337) | $ | $ | $ 9,434 | $ 644 | $ 903,896 | $ (20,662) |
| **Liabilities:** | | | | | | | | | | | | | |
| Annuity account balances (2) | $ 142,470 | $ | $ | $ 22 | $ | $ | $ | $ 161 | $ 3,508 | $ | $ | $ 139,145 | $ |
| Other liabilities (1) | 213,659 | | | 237,130 | | | 805 | | | | | 449,984 | (237,130) |
| Total liabilities measured at fair value on a recurring basis | $ 356,129 | $ | $ | $ 237,152 | $ | $ | $ 805 | $ 161 | $ 3,508 | $ | $ | $ 589,129 | $ (237,130) |

(1) Represents certain freestanding and embedded derivatives.

(2) Represents liabilities related to equity indexed annuities.

For the three months ended September 30, 2011, $9.4 million of securities were transferred into Level 3. This amount was transferred from Level 2. These transfers resulted from securities that were priced by independent pricing services or brokers in previous quarters, using no significant unobservable inputs, but were priced internally using significant unobservable inputs where market observable inputs were no longer available as of September 30, 2011.

For the three months ended September 30, 2011, there were no securities transferred out of Level 3.

For the three months ended September 30, 2011, there were no transfers from Level 2 to Level 1.

Table of Contents

The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the three months ended September 30, 2010, for which the Company has used significant unobservable inputs (Level 3):

| | | Total Realized and Unrealized Gains (losses) | | | | | |
|---|---|---|---|---|---|---|---|
| | **Beginning Balance** | **Included in Earnings** | **Included in Other Comprehensive Income** | **Purchases, Issuances, and Settlements (net)** | **Transfers in and/or out of Level 3** | **Ending Balance** | **Total Gains (losses) included in Earnings related to Instruments still held at the Reporting Date** |
| | | | | **(Dollars In Thousands)** | | | |
| **Assets:** | | | | | | | |
| Fixed maturity securities - available-for-sale | | | | | | | |
| Residential mortgage-backed securities | $ 21 | $ | $ | $ (1) | $ | $ 20 | $ |
| Commercial mortgage-backed securities | 39,952 | | 1,932 | (85) | (21,633) | 20,166 | |
| Other asset-backed securities | 597,291 | | 4,923 | 5 | | 602,219 | |
| U.S. government-related securities | 15,149 | | (29) | 3 | | 15,123 | |
| States, municipals, and political subdivisions | 82 | | | | | 82 | |
| Other government-related securities | | | | | | | |
| Corporate bonds | 108,376 | | 5,289 | 19,221 | 7,414 | 140,300 | |
| Total fixed maturity securities - available-for-sale | 760,871 | | 12,115 | 19,143 | (14,219) | 777,910 | |
| Fixed maturity securities - trading | | | | | | | |
| Residential mortgage-backed securities | | | | | | | |
| Commercial mortgage-backed securities | | | | | | | |
| Other asset-backed securities | 61,137 | 905 | | 714 | | 62,756 | 643 |
| U.S. government-related securities | 3,562 | 126 | | (2) | | 3,686 | 126 |
| States, municipals and political subdivisions | | | | | | | |
| Other government-related securities | | | | | | | |
| Corporate bonds | 43 | | | | 4,489 | 4,532 | 616 |
| Total fixed maturity securities - trading | 64,742 | 1,031 | | 712 | 4,489 | 70,974 | 1,385 |
| Total fixed maturity securities | 825,613 | 1,031 | 12,115 | 19,855 | (9,730) | 848,884 | 1,385 |
| Equity securities | 73,137 | 1,225 | 1,171 | | 5,985 | 81,518 | 1,224 |
| Other long-term investments (1) | 9,531 | 1,787 | | | | 11,318 | 1,787 |
| Short-term investments | | | | | | | |
| Total investments | 908,281 | 4,043 | 13,286 | 19,855 | (3,745) | 941,720 | 4,396 |
| Total assets measured at fair value on a recurring basis | $ 908,281 | $ 4,043 | $ 13,286 | $ 19,855 | $ (3,745) | $ 941,720 | $ 4,396 |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| **Liabilities:** | | | | | | | |
| Annuity account balances (2) | $ 149,440 | $ 2,578 | $ | $ 2,696 | $ | $ 144,166 | $ |
| Other liabilities (1) | 233,197 | (106,384) | | | | 339,581 | (106,384) |
| Total liabilities measured at fair value on a recurring basis | $ 382,637 | $ (103,806) | $ | $ 2,696 | $ | $ 483,747 | $ (106,384) |

(1) Represents certain freestanding and embedded derivatives.

(2) Represents liabilities related to equity indexed annuities.

Table of Contents

The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the nine months ended September 30, 2011, for which the Company has used significant unobservable inputs (Level 3):

| | Beginning Balance | Total Realized and Unrealized Gains Included in Earnings | Total Realized and Unrealized Gains Included in Other Comprehensive Income | Total Realized and Unrealized Losses Included in Earnings | Total Realized and Unrealized Losses Included in Other Comprehensive Income | Purchases | Sales | Issuances | Settlements | Transfers in/out of Level 3 | Other | Ending Balance | Total Gains (losses) included in Earnings related to Instruments still held at the Reporting Date |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | (Dollars In Thousands) | | | | | | | | | | | | |
| **Assets:** | | | | | | | | | | | | | |
| Fixed maturity securities available-for-sale | | | | | | | | | | | | | |
| Residential mortgage-backed securities | $ 20 | $ | $ 12 | $ (4) | $ | $ | $ (12) | $ | $ | $ (9) | $ | $ 7 | $ |
| Commercial mortgage-backed securities | 19,901 | | 147 | | | | (103) | | | (10,511) | | 9,434 | |
| Other asset-backed securities | 641,129 | 1,786 | 3,637 | (2,133) | (45,441) | 118,598 | (118,598) | | | | (137) | 598,841 | |
| U.S. government-related securities | 15,109 | | | | (119) | | | | | | 10 | 15,000 | |
| States, municipals, and political subdivisions | 78 | | | | | | (5) | | | | | 73 | |
| Other government-related securities | | | | | | | | | | | | | |
| Corporate bonds | 65,032 | | 4,873 | | (1,055) | 40,000 | (2,797) | | | 14,585 | | 120,638 | |
| Total fixed maturity securities - available-for-sale | 741,269 | 1,786 | 8,669 | (2,137) | (46,615) | 158,598 | (121,515) | | | 4,065 | (127) | 743,993 | |
| Fixed maturity securities - trading | | | | | | | | | | | | | |
| Residential mortgage-backed securities | | | | | | | | | | | | | |
| Commercial mortgage-backed securities | | | | | | | | | | | | | |
| Other asset-backed securities | 59,925 | 1,180 | | (2,230) | | 3,793 | (38,543) | | | | 2,138 | 26,263 | (656) |
| U.S. government-related securities | 3,442 | 130 | | (117) | | | | | | | (5) | 3,450 | 14 |
| States, municipals and political | | | | | | | | | | | | | |

| | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| subdivisions | | | | | | | | | | | | | |
| Other government-related securities | | | | | | | | | | | | | |
| Corporate bonds | | | | (825) | | | (71) | | | 42,041 | 81 | 41,226 | (451) |
| Total fixed maturity securities - trading | 63,367 | 1,310 | | (3,172) | | 3,793 | (38,614) | | | 42,041 | 2,214 | 70,939 | (1,093) |
| Total fixed maturity securities | 804,636 | 3,096 | 8,669 | (5,309) | (46,615) | 162,391 | (160,129) | | | 46,106 | 2,087 | 814,932 | (1,093) |
| Equity securities | 77,098 | 49 | 445 | | (1,049) | 3,962 | (49) | | | 21 | | 80,477 | |
| Other long-term investments (1) | 25,065 | | | (16,578) | | | | | | | | 8,487 | (16,577) |
| Short-term investments | | | | | | | | | | | | | |
| Total investments | 906,799 | 3,145 | 9,114 | (21,887) | (47,664) | 166,353 | (160,178) | | | 46,127 | 2,087 | 903,896 | (17,670) |
| Total assets measured at fair value on a recurring basis | $ 906,799 | $ 3,145 | $ 9,114 | $ (21,887) | $ (47,664) | $ 166,353 | $ (160,178) | $ | $ | $ 46,127 | $ 2,087 | $ 903,896 | $ (17,670) |
| **Liabilities:** | | | | | | | | | | | | | |
| Annuity account balances (2) | $ 143,264 | $ | $ | $ 4,257 | $ | $ | $ | $ 475 | $ 8,851 | $ | $ | $ 139,145 | $ |
| Other liabilities (1) | 190,529 | | | 262,128 | | | 2,673 | | | | | 449,984 | (262,128) |
| Total liabilities measured at fair value on a recurring basis | $ 333,793 | $ | $ | $ 266,385 | $ | $ | $ 2,673 | $ 475 | $ 8,851 | $ | $ | $ 589,129 | $ (262,128) |

(1) Represents certain freestanding and embedded derivatives.

(2) Represents liabilities related to equity indexed annuities.

For the nine months ended September 30, 2011, $66.1 million of securities were transferred into Level 3. This amount was transferred almost entirely from Level 2. These transfers resulted from securities that were priced by independent pricing services or brokers in previous quarters, using no significant unobservable inputs, but were priced internally using significant unobservable inputs where market observable inputs were no longer available as of September 30, 2011.

For the nine months ended September 30, 2011, $20.0 million of securities were transferred out of Level 3. This amount was transferred almost entirely to Level 2. These transfers resulted from securities that were previously valued using an internal model that utilized significant unobservable inputs but were valued internally or by independent pricing services or brokers, utilizing no significant unobservable inputs, as of September 30, 2011. All transfers are recognized as of the end of the reporting period.

For the nine months ended September 30, 2011, there were no transfers from Level 2 to Level 1.

Table of Contents

The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the nine months ended September 30, 2010, for which the Company has used significant unobservable inputs (Level 3):

| | | Total Realized and Unrealized Gains (losses) | | | | | |
|---|---|---|---|---|---|---|---|
| | Beginning Balance | Included in Earnings | Included in Other Comprehensive Income | Purchases, Issuances, and Settlements (net) | Transfers in and/or out of Level 3 | Ending Balance | Total Gains (losses) included in Earnings related to Instruments still held at the Reporting Date |
| | | | | (Dollars In Thousands) | | | |
| **Assets:** | | | | | | | |
| Fixed maturity securities - available-for-sale | | | | | | | |
| Residential mortgage-backed securities | $ 23 | $ 4 | $ | $ (7) | $ | $ 20 | $ |
| Commercial mortgage-backed securities | 844,535 | | 40,213 | (842,949)(3) | (21,633) | 20,166 | |
| Other asset-backed securities | 693,930 | 5,868 | 1,227 | (89,468) | (9,338) | 602,219 | |
| U.S. government-related securities | 15,102 | | 11 | 10 | | 15,123 | |
| States, municipals, and political subdivisions | 86 | | | (4) | | 82 | |
| Other government-related securities | | | | | | | |
| Corporate bonds | 86,328 | | 8,454 | 37,954 | 7,564 | 140,300 | |
| Total fixed maturity securities - available-for-sale | 1,640,004 | 5,872 | 49,905 | (894,464) | (23,407) | 777,910 | |
| Fixed maturity securities - trading | | | | | | | |
| Residential mortgage-backed securities | 7,244 | (1) | | (3,855) | (3,388) | | |
| Commercial mortgage-backed securities | | | | | | | |
| Other asset-backed securities | 47,509 | 150 | | 15,097 | | 62,756 | (377) |
| U.S. government-related securities | 3,310 | 381 | | (5) | | 3,686 | 381 |
| States, municipals, and political subdivisions | 4,994 | 77 | | | (5,071) | | |
| Other government-related securities | 41,965 | 1,058 | | (47) | (42,976) | | |
| Corporate bonds | 67 | 323 | | 26,786 | (22,644) | 4,532 | 616 |
| Total fixed maturity securities - trading | 105,089 | 1,988 | | 37,976 | (74,079) | 70,974 | 620 |
| Total fixed maturity securities | 1,745,093 | 7,860 | 49,905 | (856,488) | (97,486) | 848,884 | 620 |
| Equity securities | 70,708 | 1,229 | 1,171 | 2,425 | 5,985 | 81,518 | 1,224 |
| Other long-term investments (1) | 16,525 | (5,207) | | | | 11,318 | (5,207) |
| Short-term investments | | | | | | | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Total investments | 1,832,326 | 3,882 | 51,076 | (854,063) | (91,501) | 941,720 | (3,363) |
| Total assets measured at fair value on a recurring basis | $ 1,832,326 | $ 3,882 | $ 51,076 | $ (854,063) | $ (91,501) | $ 941,720 | $ (3,363) |
| **Liabilities:** | | | | | | | |
| Annuity account balances (2) | $ 149,893 | $ (263) | $ | $ 5,990 | $ | $ 144,166 | $ |
| Other liabilities (1) | 105,838 | (233,743) | | | | 339,581 | (233,743) |
| Total liabilities measured at fair value on a recurring basis | $ 255,731 | $ (234,006) | $ | $ 5,990 | $ | $ 483,747 | $ (233,743) |

(1) Represents certain freestanding and embedded derivatives.
(2) Represents liabilities related to equity indexed annuities.
(3) Represents mortgage loan held by the trusts that have been consolidated upon the adoption of ASU No. 2009-17.

Total realized and unrealized gains (losses) on Level 3 assets and liabilities are primarily reported in either realized investment gains (losses) within the consolidated statements of income (loss) or other comprehensive income (loss) within shareowners equity based on the appropriate accounting treatment for the item.

Purchases, sales, issuances, and settlements, net, represent the activity that occurred during the period that results in a change of the asset or liability but does not represent changes in fair value for the instruments held at the beginning of the period. Such activity primarily relates to purchases and sales of fixed maturity securities and issuances and settlements of equity indexed annuities.

The Company reviews the fair value hierarchy classifications each reporting period. Changes in the observability of the valuation attributes may result in a reclassification of certain financial assets or liabilities. Such reclassifications are reported as transfers in and out of Level 3 at the beginning fair value for the reporting period in which the changes occur. The asset transfers in the table(s) above primarily related to positions moved from Level 3 to Level 2 as the Company determined that certain inputs were observable.

The amount of total gains (losses) for assets and liabilities still held as of the reporting date primarily represents changes in fair value of trading securities and certain derivatives that exist as of the reporting date and the change in fair value of equity indexed annuities.

Table of Contents

***Estimated Fair Value of Financial Instruments***

The carrying amounts and estimated fair values of the Company s financial instruments as of the periods shown below are as follows:

| | As of | | | |
|---|---|---|---|---|
| | September 30, 2011 | | December 31, 2010 | |
| | Carrying Amounts | Fair Values | Carrying Amounts | Fair Values |
| | (Dollars In Thousands) | | | |
| **Assets:** | | | | |
| Mortgage loans on real estate | $ 5,377,977 | $ 6,270,590 | $ 4,892,829 | $ 5,336,732 |
| Policy loans | 880,203 | 880,203 | 793,448 | 793,448 |
| **Liabilities:** | | | | |
| Stable value product account balances | $ 2,827,862 | $ 2,923,560 | $ 3,076,233 | $ 3,163,902 |
| Annuity account balances | 10,975,016 | 10,836,441 | 10,591,605 | 10,451,526 |
| Mortgage loan backed certificates | 32,471 | 32,877 | 61,678 | 63,127 |
| **Debt:** | | | | |
| Bank borrowings | $ 145,000 | $ 145,000 | $ 142,000 | $ 142,000 |
| Senior and Medium-Term Notes | 1,350,000 | 1,487,636 | 1,359,852 | 1,455,641 |
| Subordinated debt securities | 524,743 | 521,315 | 524,743 | 517,383 |
| Non-recourse funding obligations | 414,800 | 227,434 | 532,400 | 389,534 |

Except as noted below, fair values were estimated using quoted market prices.

**Fair Value Measurements**

***Mortgage loans on real estate***

The Company estimates the fair value of mortgage loans using an internally developed model. This model includes inputs derived by the Company based on assumed discount rates relative to the Company s current mortgage loan lending rate and an expected cash flow analysis based on a review of the mortgage loan terms. The model also contains the Company s determined representative risk adjustment assumptions related to nonperformance and liquidity risks.

***Policy loans***

The Company believes the fair value of policy loans approximates book value. Policy loans are funds provided to policy holders in return for a claim on the policy. The funds provided are limited to the cash surrender value of the underlying policy. The nature of policy loans is to have a

negligible default risk as the loans are fully collateralized by the value of the policy. Policy loans do not have a stated maturity and the balances and accrued interest are repaid either by the policyholder or with proceeds from the policy. Due to the collateralized nature of policy loans and unpredictable timing of repayments, the Company believes the fair value of policy loans approximates carrying value.

***Stable value product and Annuity account balances***

The Company estimates the fair value of stable value product account balances and annuity account balances using models based on discounted expected cash flows. The discount rates used in the models were based on a current market rate for similar financial instruments.

***Bank borrowings***

The Company believes the carrying value of its bank borrowings approximates fair value.

Table of Contents

*Non-recourse funding obligations*

As of September 30, 2011, the Company estimated the fair value of its non-recourse funding obligations using internal discounted cash flow models. The discount rates used in the model were based on a current market yield for similar financial instruments.

**15. DERIVATIVE FINANCIAL INSTRUMENTS**

**Types of Derivative Instruments and Derivative Strategies**

The Company utilizes a risk management strategy that incorporates the use of derivative financial instruments to reduce exposure to interest rate risk, inflation risk, currency exchange risk, volatility risk, and equity market risk. These strategies are developed through the Company s analysis of data from financial simulation models and other internal and industry sources, and are then incorporated into the Company s risk management program.

Derivative instruments expose the Company to credit and market risk and could result in material changes from period to period. The Company attempts to minimize its credit risk by entering into transactions with highly rated counterparties. The Company manages the market risk by establishing and monitoring limits as to the types and degrees of risk that may be undertaken. The Company monitors its use of derivatives in connection with its overall asset/liability management programs and risk management strategies. In addition, all derivative programs are monitored by our risk management department.

***Derivatives Related to Interest Rate Risk Management***

Derivative instruments that are used as part of the Company s interest rate risk management strategy include interest rate swaps, interest rate futures, interest rate options, interest rate caps, and interest rate swaptions. The Company s inflation risk management strategy involves the use of swaps that requires the Company to pay a fixed rate and receive a floating rate that is based on changes in the Consumer Price Index ( CPI ).

***Derivatives Related to Risk Mitigation of Variable Annuity Contracts***

The Company uses the following types of derivative contracts to mitigate its exposure to certain guaranteed benefits related to variable annuity contracts:

- Foreign Currency Futures

- Variance Swaps
- Interest Rate Futures
- Equity Options
- Equity Futures
- Credit Derivatives

The Company has sold credit protection under single name credit default swaps and credit default swap indices for which it receives a premium to insure credit risk. Such credit derivatives are a part of the Company s program to mitigate risks related to certain minimum guaranteed benefits of variable annuity contracts and are designed to offset some portion of the Company s nonperformance risk. The Company will only make a payment in the event there is a credit event. A credit event payment will typically be equal to the notional value of the swap contract less an auction-determined recovery rate, to the percentage extent described. A credit event is generally defined to include material default, bankruptcy, or debt restructuring. The Company s maximum amount at risk, assuming the value of all referenced credit obligations is zero, equals the notional value of the credit default swaps.

Table of Contents

The following table includes the estimated fair value, maximum amount of future payments, and the maturity dates of written credit default swaps, segregated by counterparty exposure:

| Maturity | Reason for entering | Nature of recourse | Number of instruments | Fair Value(3) | Upfront fee received | Unrealized gain (loss) | Maximum potential payout(4) |
|---|---|---|---|---|---|---|---|
| | | | (Dollars In Thousands) | | | | |
| 12/20/21 | (1) | (2) | 3 | (35,883) | 29,515 | (6,368) | 700,000(5) |
| 12/20/21 | (1) | (2) | 1 | (9,934) | 8,153 | (1,781) | 200,000 |
| 12/20/21 | (1) | (2) | 1 | (4,823) | 4,990 | 167 | 100,000 |
| | | | 5 | (50,640) | 42,658 | (7,982) | 1,000,000 |

(1) The Company wrote these positions to mitigate the Company s non-performance risk related to certain guaranteed minimum withdrawal benefits within its variable annuity products.

(2) The Company does not have the right to demand indemnification or compensation from third parties in the case of a loss (payment) on the contract.

(3) Broker quotes are used to determine the market value of credit derivatives.

(4) The underlying reference entity is the Markit CDX North America Investment Grade Index, Series 17, which is comprised of 125 equally weighted credit default swaps on investment grade entities. The maximum potential payout assumes the recovery value on each investment grade entity is zero.

(5) The Company has posted $20 million of collateral with this counterparty for over-the-counter derivative positions.

The following table includes the credit ratings of the underlying entities that make up the index as of September 30, 2011:

| Rating | Credit rating of underlying index |
|---|---|
| AA | 4.0% |
| A | 34.0 |
| BBB | 62.0 |
| | 100.0% |

**Accounting for Derivative Instruments**

The Company records its derivative instruments in the consolidated balance sheet in other long-term investments and other liabilities in accordance with GAAP, which requires that all derivative instruments be recognized in the balance sheet at fair value. The accounting for changes in fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship in accordance with GAAP.

For those derivative instruments that are designated and qualify as hedging instruments, a company must designate the hedging instrument, based upon the exposure being hedged, as a fair value hedge, cash flow hedge, or a hedge related to foreign currency exposure. For derivatives that are designated and qualify as cash flow hedges, the effective portion of the gain or loss realized on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged transaction impacts earnings. The remaining gain or loss on these derivatives is recognized as ineffectiveness in current earnings during the period of the change. For derivatives that are designated and qualify as fair value hedges, the gain or loss on the derivative instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings during the period of change in fair values. Effectiveness of the Company s hedge relationships is assessed on a quarterly basis.

The Company accounts for changes in fair values of derivatives that are not part of a qualifying hedge relationship through earnings in the period of change. Changes in the fair value of derivatives that are recognized in current earnings are reported in realized investment gains (losses) derivative financial instruments .

Table of Contents

**Derivative Instruments Designated and Qualify as Hedging Instruments**

**Cash-Flow Hedges**

- In connection with the issuance of inflation adjusted funding agreements, the Company has entered into swaps to convert the floating CPI-linked interest rate on the contracts to a fixed rate. The Company paid a fixed rate on the swap and received a floating rate equal to the CPI change paid on the funding agreements.

- The Company has entered into an interest rate swap to convert LIBOR based floating rate interest payments on funding agreement to fixed rate interest payments.

**Derivative Instruments Not Designated and Not Qualifying as Hedging Instruments**

The Company also uses various other derivative instruments for risk management purposes that either do not qualify for hedge accounting treatment or have not currently been designated by the Company for hedge accounting treatment. Changes in the fair value of these derivatives are recognized in earnings during the period of change.

**Derivatives related to variable annuity contracts**

- The Company uses equity, interest rate, and currency futures to mitigate the interest rate risk related to certain guaranteed minimum benefits within our variable annuity products. In general, the cost of such benefits varies with the level of equity and interest rate markets and overall volatility. The equity futures resulted in a net pre-tax gain of $11.5 million and a pre-tax loss of $7.8 million, interest rate futures resulted in pre-tax gains of $144.2 million and $147.6 million, and currency futures resulted in net pre-tax gains of $2.4 million and $2.2 million, for the three and nine months ended September 30, 2011, respectively.

- The Company uses equity options, volatility swaps, and interest rate swaps to mitigate the risk related to certain guaranteed minimum benefits, including guaranteed minimum withdrawal benefits, within our variable annuity products. In general, the cost of such benefits varies with the level of equity and interest rate markets and overall volatility. The equity options resulted in net pre-tax gains of $30.1 million and $22.8 million, the volatility swaps resulted in net pre-tax gains of $3.5 million and a loss of $0.2 million, and the interest rate swaps resulted in a net pre-tax gain of $5.8 million and $5.8 million for the three and nine months ended September 30, 2011, respectively. Such positions were not held during the nine months ended September 30, 2010.

- The Company entered into credit default swaps to partially mitigate the Company s non-performance risk related to certain guaranteed minimum withdrawal benefits within our variable annuity products. The Company reported net pre-tax losses of $24.0 million and $23.0 million for the three and nine months ended September 30, 2011 related to credit default swaps from the change in swaps fair value premium income, and a realized loss on terminated contracts of $17.6 million.

- The Company markets certain variable annuity products with a GMWB rider. The GMWB component is considered an embedded derivative, not considered to be clearly and closely related to the host contract. The Company recognized pre-tax losses of $150.1 million and $147.6 million for the three and nine months ended September 30, 2011, and pre-tax losses of $19.1 million and $59.3 million for the three and nine months ended September 30, 2010, respectively, related to these embedded derivatives.

**Other Derivatives**

- The Company entered into credit default swaps to enhance the return on its investment portfolio. The Company reported net pre-tax losses of $0.3 million and $0.5 million for the three and nine months ended September 30, 2011, and pre-tax gains of $1.0 million and $0.4 million for the three and nine months ended September 30 2010, respectively, related to credit default swaps from the change in swaps fair value and premium income.

- The Company uses certain interest rate swaps to mitigate the price volatility of fixed maturities. The Company recognized pre-tax losses of $8.2 million and $10.6 million on interest rate swaps for the

Table of Contents

three and nine months ended September 30, 2011 and pre-tax losses of $4.7 million and $13.5 million on interest rate swaps for the three and nine months ended September 30, 2010, respectively.

- The Company purchased interest rate caps in the three months ended September 30, 2011. These caps mitigate the Company s credit risk with respect to its holding of the debt of certain European banks. These banks in turn hold sovereign debt of certain European governments. These caps resulted in net pre-tax losses of $2.6 million for the three and nine months ended September 30, 2011.

- The Company uses other types of derivatives to manage risk related to other exposures. The Company recognized pre-tax losses of $0.6 million for the three and nine months ended September 30, 2011. The Company recognized losses of $0.4 million for the three months ended September 30, 2010 and pre-tax gains of $0.4 million for the nine months ended September 30, 2010.

- The Company is involved in various modified coinsurance and funds withheld arrangements which contain embedded derivatives that must be reported at fair value. Changes in fair value are recorded in current period earnings. The investment portfolios that support the related modified coinsurance reserves and funds withheld arrangements had mark-to-market changes which substantially offset the gains or losses on these embedded derivatives. The Company recognized pre-tax losses of $109.5 million and $130.9 million for the three and nine months ended September 30, 2011 and pre-tax losses of $85.5 million and $179.7 million for the three and nine months ended September 30, 2010, respectively.

Table of Contents

The tables below present information about the nature and accounting treatment of the Company s primary derivative financial instruments and the location in and effect on the consolidated condensed financial statements for the periods presented below:

| | As of September 30, 2011 | | As of December 31, 2010 | |
|---|---|---|---|---|
| | Notional Amount | Fair Value | Notional Amount | Fair Value |
| | (Dollars In Thousands) | | | |
| Other long-term investments | | | | |
| Cash flow hedges: | | | | |
| Inflation | $ 12,084 | $ 3 | $ | $ |
| Derivatives not designated as hedging instruments: | | | | |
| Interest rate swaps | 100,000 | 5,808 | 25,000 | 3,808 |
| Credit default swaps | | | | |
| Embedded derivative - Modco reinsurance treaties | 29,964 | 2,173 | 29,563 | 2,687 |
| Embedded derivative - GMWB | 685,478 | 6,314 | 1,099,902 | 22,378 |
| Interest rate futures | 1,246,697 | 51,748 | | |
| Equity futures | 231,664 | 10,102 | | |
| Currency futures | 74,661 | 2,071 | | |
| Interest rate caps | 3,000,000 | 2,885 | | |
| Other | 505,214 | 27,922 | 95,000 | 6,794 |
| | $ 5,885,762 | $ 109,026 | $ 1,249,465 | $ 35,667 |
| Other liabilities | | | | |
| Cash flow hedges: | | | | |
| Inflation | $ 251,467 | $ 11,727 | $ 293,379 | $ 12,005 |
| Interest rate | 75,000 | 3,415 | 75,000 | 6,747 |
| Derivatives not designated as hedging instruments: | | | | |
| Credit default swaps | 1,000,000 | 50,640 | 25,000 | 1,099 |
| Interest rate swaps | 25,000 | 2,817 | 110,000 | 9,137 |
| Embedded derivative - Modco reinsurance treaties | 2,787,486 | 276,508 | 2,842,862 | 146,105 |
| Embedded derivative - GMWB | 3,484,749 | 173,476 | 1,494,657 | 41,990 |
| Interest rate futures | 113,536 | 133 | 598,357 | 16,764 |
| Equity futures | | | 327,321 | 7,231 |
| Other | | | 338,438 | 2,433 |
| | $ 7,737,238 | $ 518,716 | $ 6,105,014 | $ 243,511 |

**Gain (Loss) on Derivatives in Cash Flow Hedging Relationship**

| | For The Three Months Ended September 30, 2011 | | | For The Nine Months Ended September 30, 2011 | | |
|---|---|---|---|---|---|---|
| | Realized investment gains (losses) | Benefits and settlement expenses | Other comprehensive income (loss) | Realized investment gains (losses) | Benefits and settlement expenses | Other comprehensive income (loss) |
| | (Dollars In Thousands) | | | | | |
| **Gain (loss) recognized in other comprehensive income (loss)** (effective portion): | | | | | | |
| Interest rate | $ | $ | $ 38 | $ | $ | $ (304) |
| Inflation | | | (3,162) | | | (978) |

| | | | | | | |
|---|---|---|---|---|---|---|
| **Gain (loss) reclassified from accumulated other comprehensive income (loss) into income** (effective portion): | | | | | | |
| Interest rate | $ | $ (911) | $ | $ | $ (2,689) | $ |
| Inflation | | 488 | | | (840) | |
| **Gain (loss) recognized in income** (ineffective portion): | | | | | | |
| Inflation | $ (485) | $ | $ | $ (457) | $ | $ |

Table of Contents

**Gain (Loss) on Derivatives in Cash Flow Hedging Relationship**

| | For The Three Months Ended September 30, 2010 | | | For The Nine Months Ended September 30, 2010 | | |
|---|---|---|---|---|---|---|
| | Realized investment gains (losses) | Benefits and settlement expenses | Other comprehensive income (loss) | Realized investment gains (losses) | Benefits and settlement expenses | Other comprehensive income (loss) |
| | (Dollars In Thousands) | | | | | |
| **Gain (loss) recognized in other comprehensive income (loss)** (effective portion): | | | | | | |
| Interest rate | $ | $ | $ (842) | $ | $ | $ (2,958) |
| Inflation | | | 1,532 | | | (2,360) |
| **Gain (loss) reclassified from accumulated other comprehensive income (loss) into income** (effective portion): | | | | | | |
| Interest rate | $ | $ (1,774) | $ | $ | $ (5,747) | $ |
| Inflation | | (965) | | | (2,049) | |
| **Gain (loss) recognized in income** (ineffective portion): | | | | | | |
| Inflation | $ 25 | $ | $ | $ (311) | $ | $ |

Based on the expected cash flows of the underlying hedged items, the Company expects to reclassify $3.9 million out of accumulated other comprehensive income (loss) into earnings during the next twelve months.

**Realized investment gains (losses) - derivative financial instruments**

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands) | | | |
| Derivatives related to variable annuity contracts: | | | | |
| Interest rate futures - VA | $ 144,182 | $ 23,047 | $ 147,550 | $ 23,047 |
| Equity futures - VA | 11,524 | (8,444) | (7,822) | (8,444) |
| Currency futures - VA | 2,376 | | 2,177 | |
| Volatility swaps - VA | 3,495 | | (239) | |
| Equity options - VA | 30,072 | | 22,813 | |
| Interest rate swaps - VA | 5,808 | | 5,808 | |
| Credit default swaps - VA | (23,897) | | (22,981) | |
| Embedded derivative - GMWB | (150,125) | (19,101) | (147,550) | (59,296) |
| Total derivatives related to variable annuity contracts | 23,435 | (4,498) | (244) | (44,693) |
| Embedded derivative - Modco reinsurance treaties | (109,542) | (85,496) | (130,914) | (179,654) |
| Interest rate swaps | (8,185) | (4,676) | (10,642) | (13,450) |
| Interest rate caps | (2,581) | | (2,581) | |
| Credit default swaps | (321) | 1,040 | (543) | 404 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Other | | (622) | | (404) | | (571) | | 399 |
| Total realized gains (losses) - derivatives | $ | (97,816) | $ | (94,034) | $ | (145,495) | $ | (236,994) |

**Realized investment gains (losses) - all other investments**

| | For The Three Months Ended September 30, | | | | For The Nine Months Ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | 2011 | | 2010 | | 2011 | | 2010 | |
| | (Dollars In Thousands) | | | | | | | |
| Modco trading portfolio(1) | $ | 123,760 | $ | 96,689 | $ | 151,714 | $ | 204,749 |

(1) The Company elected to include the use of alternate disclosures for trading activities.

Table of Contents

**16. OPERATING SEGMENTS**

The Company has several operating segments each having a strategic focus. An operating segment is distinguished by products, channels of distribution, and/or other strategic distinctions. The Company periodically evaluates its operating segments, as prescribed in the ASC Segment Reporting Topic, and makes adjustments to its segment reporting as needed. A brief description of each segment follows.

- The Life Marketing segment markets universal life ( UL ), variable universal life, bank-owned life insurance ( BOLI ), and level premium term insurance ( traditional ) products on a national basis primarily through networks of independent insurance agents and brokers, stockbrokers, and independent marketing organizations.

- The Acquisitions segment focuses on acquiring, converting, and servicing policies acquired from other companies. The segment s primary focus is on life insurance policies and annuity products that were sold to individuals. In the ordinary course of business, the Acquisitions segment regularly considers acquisitions of blocks of policies or insurance companies. The level of the segment s acquisition activity is predicated upon many factors, including available capital, operating capacity, and market dynamics. Policies acquired through the Acquisitions segment are typically closed blocks of business (no new policies are being marketed). Therefore, in such instances, earnings and account values are expected to decline as the result of lapses, deaths, and other terminations of coverage unless new acquisitions are made.

- The Annuities segment markets fixed and variable annuity products. These products are primarily sold through broker-dealers, financial institutions, and independent agents and brokers.

- The Stable Value Products segment sells guaranteed funding agreements ( GFAs ) to special purpose entities that in turn issue notes or certificates in smaller, transferable denominations. The segment also markets fixed and floating rate funding agreements directly to the trustees of municipal bond proceeds, institutional investors, bank trust departments, and money market funds. In addition, the segment issues funding agreements to the FHLB, and markets guaranteed investment contracts ( GICs ) to 401(k) and other qualified retirement savings plans.

- The Asset Protection segment markets extended service contracts and credit life and disability insurance to protect consumers investments in automobiles, watercraft, and recreational vehicles. In addition, the segment markets a guaranteed asset protection ( GAP ) product. GAP coverage covers the difference between the loan pay-off amount and an asset s actual cash value in the case of a total loss.

- The Corporate and Other segment primarily consists of net investment income (including the impact of carrying excess liquidity), expenses not attributable to the segments above (including interest on debt), and a trading portfolio that was previously part of a variable interest entity. This segment includes earnings from several non-strategic or runoff lines of business, various investment-related transactions, the operations of several small subsidiaries, and the repurchase of non-recourse funding obligations.

The Company uses the same accounting policies and procedures to measure segment operating income (loss) and assets as it uses to measure consolidated net income available to PLC s common shareowners and assets. Segment operating income (loss) is income before income tax excluding net realized investment gains and losses (net of the related amortization of deferred acquisition costs ( DAC ) and value of business acquired ( VOBA ) and participating income from real estate ventures), and the cumulative effect of change in accounting principle. Periodic settlements of derivatives associated with corporate debt and certain investments and annuity products are included in realized gains and losses but are considered part of operating income because the derivatives are used to mitigate risk in items affecting consolidated and segment operating income (loss). Segment operating income (loss) represents the basis on which the performance of the Company s business is internally assessed by management. Premiums and policy fees, other income, benefits and settlement expenses, and amortization of DAC/VOBA are attributed directly to each operating segment. Net investment income is allocated based on directly related assets required for transacting the business of that segment. Realized investment gains (losses) and other operating expenses are allocated to the segments in a manner that most appropriately reflects the operations of that segment. Investments and other assets are allocated based on statutory policy liabilities net of associated statutory policy assets, while DAC/VOBA and goodwill are shown in the segments to which they are attributable.

During the first quarter of 2010, the Company recorded a $7.8 million decrease in reserves related to the final settlement in the runoff Lender s Indemnity line of business.

Table of Contents

During the first quarter of 2011, the Company recorded $8.5 million of pre-tax earnings in the Corporate and Other business segment relating to the settlement of a dispute with respect to certain investments.

There were no significant intersegment transactions during the nine months ended September 30, 2011 and 2010.

The following tables summarize financial information for the Company s segments:

| | For The Three Months Ended September 30, | | For The Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| | (Dollars In Thousands) | | | |
| **Revenues** | | | | |
| Life Marketing | $ 331,239 | $ 309,986 | $ 988,003 | $ 917,118 |
| Acquisitions | 273,066 | 188,177 | 715,960 | 564,473 |
| Annuities | 183,201 | 141,129 | 466,935 | 367,184 |
| Stable Value Products | 45,158 | 42,031 | 136,294 | 127,260 |
| Asset Protection | 71,289 | 67,756 | 208,969 | 201,956 |
| Corporate and Other | 35,428 | 54,022 | 163,084 | 128,982 |
| Total revenues | $ 939,381 | $ 803,101 | $ 2,679,245 | $ 2,306,973 |
| **Segment Operating Income (Loss)** | | | | |
| Life Marketing | $ 20,321 | $ 30,868 | $ 80,264 | $ 107,301 |
| Acquisitions | 44,028 | 27,866 | 115,848 | 89,425 |
| Annuities | 43,784 | 22,704 | 81,244 | 41,496 |
| Stable Value Products | 14,217 | | | |