PROTECTIVE LIFE CORP
Form 10-Q
November 04, 2010
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

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, 2010

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)

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 29, 2010: 85,666,562

Table of Contents

PROTECTIVE LIFE CORPORATION

QUARTERLY REPORT ON FORM 10-Q

FOR QUARTERLY PERIOD ENDED SEPTEMBER 30, 2010

TABLE OF CONTENTS

		Page
	PART I: Financial Information	
Item 1.	Financial Statements (unaudited):	
	Consolidated Condensed Statements of Income For The Three and Nine Months Ended September 30, 2010 and 2009	3
	Consolidated Condensed Balance Sheets as of September 30, 2010 and December 31, 2009	4
	Consolidated Condensed Statement of Shareowners Equity For The Nine Months Ended September 30, 2010	5
	Consolidated Condensed Statements of Cash Flows For The Nine Months Ended September 30, 2010 and 2009	7
	Notes to Consolidated Condensed Financial Statements	8
Item 2.	Management s Discussion and Analysis of Financial Condition and Results of Operations	41
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	101
Item 4.	Controls and Procedures	101
	PART II	
Item 1A.	Risk Factors and Cautionary Factors that may Affect Future Results	102
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	108
Item 6.	Exhibits	108
	Signature	109

Table of Contents

PROTECTIVE LIFE CORPORATION

CONSOLIDATED CONDENSED STATEMENTS OF INCOME

(Unaudited)

	For The Three Months Ended September 30, 2010	For The Three Months Ended September 30, 2009	For The Nine Months Ended September 30, 2010	For The Nine Months Ended September 30, 2009
	(Dollars In Thousands, Except Per Share Amounts)			
Revenues				
Premiums and policy fees	$ 640,265	$ 652,497	$ 1,948,278	$ 1,991,638
Reinsurance ceded	(334,040)	(351,664)	(1,019,598)	(1,104,188)
Net of reinsurance ceded	306,225	300,833	928,680	887,450
Net investment income	429,548	409,956	1,264,045	1,262,785
Realized investment gains (losses):				
Derivative financial instruments	(94,034)	(195,540)	(236,994)	(201,098)
All other investments	110,787	165,576	226,390	291,532
Other-than-temporary impairment losses	(12,898)	(14,873)	(71,437)	(181,064)
Portion of loss recognized in other comprehensive income (before taxes)	5,283	(16,095)	35,155	19,299
Net impairment losses recognized in earnings	(7,615)	(30,968)	(36,282)	(161,765)
Other income	58,190	41,222	161,134	119,471
Total revenues	803,101	691,079	2,306,973	2,198,375
Benefits and expenses				
Benefits and settlement expenses, net of reinsurance ceded: (three months: 2010 - $308,594; 2009 - $308,979; nine months: 2010 - $971,061; 2009 - $1,014,907)	549,567	521,218	1,582,233	1,503,725
Amortization of deferred policy acquisition costs and value of business acquired	42,386	47,240	146,761	250,837
Other operating expenses, net of reinsurance ceded: (three months: 2010 - $48,851; 2009 - $54,791; nine months: 2010 - $142,932; 2009 - $161,819)	104,151	80,985	305,246	229,803
Total benefits and expenses	696,104	649,443	2,034,240	1,984,365
Income before income tax	106,997	41,636	272,733	214,010
Income tax expense	36,626	14,051	91,412	73,533
Net income	70,371	27,585	181,321	140,477
Less: Net income (loss) attributable to noncontrolling interests	(77)		(277)	
Net income available to PLC s common shareowners(1)	$ 70,448	$ 27,585	$ 181,598	$ 140,477
Net income available to PLC s common shareowners - basic	$ 0.81	$ 0.32	$ 2.10	$ 1.79
Net income available to PLC s common shareowners - diluted	$ 0.80	$ 0.32	$ 2.07	$ 1.77
Cash dividends paid per share	$ 0.14	$ 0.12	$ 0.40	$ 0.36
Average shares outstanding - basic	86,603,569	86,481,240	86,555,761	78,465,685
Average shares outstanding - diluted	87,701,592	87,372,659	87,640,221	79,156,305

(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, 2010	December 31, 2009
	(Dollars In Thousands)	
Assets		
Fixed maturities, at fair value (amortized cost: 2010 - $23,605,857; 2009 - $23,228,317)	$ 24,838,626	$ 22,830,427
Equity securities, at fair value (cost: 2010 - $327,045; 2009 - $280,615)	335,151	275,497
Mortgage loans (2010 includes: $951,105 related to securitizations)	4,884,102	3,877,087
Investment real estate, net of accumulated depreciation (2010 - $1,073; 2009 - $803)	24,669	25,188
Policy loans	767,214	794,276
Other long-term investments	256,093	204,754
Short-term investments	483,698	1,049,609
Total investments	31,589,553	29,056,838
Cash	151,340	205,325
Accrued investment income	320,668	285,350
Accounts and premiums receivable, net of allowance for uncollectible amounts (2010 - $4,570; 2009 - $5,170)	65,948	56,216
Reinsurance receivables	5,563,824	5,333,401
Deferred policy acquisition costs and value of business acquired	3,642,484	3,663,350
Goodwill	115,532	117,856
Property and equipment, net of accumulated depreciation (2010 - $128,947; 2009 - $123,709)	37,722	37,037
Other assets	207,198	176,303
Income tax receivable	2,438	115,447
Assets related to separate accounts		
Variable annuity	3,899,308	2,948,457
Variable universal life	336,299	316,007
Total Assets	$ 45,932,314	$ 42,311,587
Liabilities		
Policy liabilities and accruals	$ 19,129,506	$ 18,548,267
Stable value product account balances	3,105,822	3,581,150
Annuity account balances	10,451,322	9,911,040
Other policyholders funds	577,275	515,078
Other liabilities	1,115,755	715,110
Mortgage loan backed certificates	74,324	
Deferred income taxes	1,113,532	553,062
Non-recourse funding obligations	548,000	575,000
Long-term debt	1,485,852	1,644,852
Subordinated debt securities	524,743	524,743
Liabilities related to separate accounts		
Variable annuity	3,899,308	2,948,457
Variable universal life	336,299	316,007
Total liabilities	42,361,738	39,832,766
Commitments and contingencies - Note 7		
Shareowners equity		
Preferred Stock, $1 par value, shares authorized: 4,000,000; Issued: None		
Common Stock, $.50 par value, shares authorized: 2010 and 2009 - 160,000,000; shares issued: 2010 and 2009 - 88,776,960	44,388	44,388

Additional paid-in-capital		584,865		576,887
Treasury stock, at cost (2010 - 3,112,442 shares; 2009 - 3,196,157 shares)		(26,101)		(25,929)
Retained earnings		2,366,276		2,204,644
Accumulated other comprehensive income (loss):				
Net unrealized gains (losses) on investments, net of income tax: (2010 -$364,723; 2009 - $(121,737))		677,343		(225,648)
Net unrealized (losses) gains relating to other-than-temporary impaired investments for which a portion has been recognized in earnings, net of income tax: (2010 - $(7,698); 2009 - $(16,704))		(14,296)		(31,021)
Accumulated loss - derivatives, net of income tax: (2010 - $(9,002); 2009 - $(10,182))		(16,718)		(18,327)
Postretirement benefits liability adjustment, net of income tax: (2010 -$(23,889); 2009 - $(24,862))		(44,365)		(46,173)
Total Protective Life Corporation s shareowners equity		3,571,392		2,478,821
Noncontrolling interest		(816)		
Total equity		3,570,576		2,478,821
Total liabilities and shareowners equity	$	45,932,314	$	42,311,587

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 Other Comprehensive Income (Loss): 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, 2009	$ 44,388	$ 576,887	$ (25,929)	$ 2,204,644	$ (256,669)	$ (18,327)	$ (46,173)	$ 2,478,821	$	$ 2,478,821
Net income for the three months ended March 31, 2010				69,779				69,779	(73)	69,706
Change in net unrealized gains/losses on investments (net of income tax - $142,481)					263,959			263,959		263,959
Reclassification adjustment for investment amounts included in net income (net of income tax - $1,725)					3,418			3,418		3,418
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 $(3,495))					(6,492)			(6,492)		(6,492)
Change in accumulated gain (loss) derivatives (net of income tax - $3,423)						5,718		5,718		5,718
Reclassification adjustment for derivative amounts included in net income (net of income tax - $(974))						(1,752)		(1,752)		(1,752)
Change in minimum pension liability adjustment (net of income tax - $324)							602	602		602
Comprehensive income for the three months ended March 31, 2010								335,232	(73)	335,159
Cash dividends ($0.120 per share)				(10,270)				(10,270)		(10,270)
Cumulative effect adjustments				14,290				14,290		14,290
Noncontrolling interest									(418)	(418)
Stock-based compensation		3,028	(68)					2,960		2,960
Balance, March 31, 2010	$ 44,388	$ 579,915	$ (25,997)	$ 2,278,443	$ 4,216	$ (14,361)	$ (45,571)	$ 2,821,033	$ (491)	$ 2,820,542
Net income for the three months ended June 30, 2010				41,371				41,371	(127)	41,244
Change in net unrealized gains/losses on investments (net of income tax - $130,774)					242,856			242,856		242,856
Reclassification adjustment for investment amounts included in net income (net of income tax - $3,894)					7,241			7,241		7,241
Change in net unrealized gains/losses relating to other-than-temporary impaired					(12,924)			(12,924)		(12,924)

investments for which a portion has been recognized in earnings (net of income tax $(6,960))										
Change in accumulated gain (loss) derivatives (net of income tax - $(3,229))						(5,952)		(5,952)		(5,952)
Reclassification adjustment for derivative amounts included in net income (net of income tax - $768)						1,382		1,382		1,382
Change in minimum pension liability adjustment (net of income tax - $325)							603	603		603
Comprehensive income for the three months ended June 30, 2010								274,577	(127)	274,450
Cash dividends ($0.14 per share)				(11,994)				(11,994)		(11,994)
Cumulative effect adjustments										
Noncontrolling interest									(121)	(121)
Stock-based compensation		1,731	252					1,983		1,983
Balance, June 30, 2010	$ 44,388	$ 581,646	$ (25,745)	$ 2,307,820	$ 241,389	$ (18,931)	$ (44,968)	$ 3,085,599	$ (739)	$ 3,084,860

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, 2010				70,448				70,448	(77)	70,371
Change in net unrealized gains/losses on investments (net of income tax - $211,169)					392,180			392,180		392,180
Reclassification adjustment for investment amounts included in net income (net of income tax - $(3,583))					(6,663)			(6,663)		(6,663)
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 $19,461)					36,141			36,141		36,141
Change in accumulated gain (loss) derivatives (net of income tax - $1,951)						3,581		3,581		3,581
Reclassification adjustment for derivative amounts included in net income (net of income tax - $(760))						(1,368)		(1,368)		(1,368)
Change in minimum pension liability adjustment (net of income tax - $325)							603	603		603
Comprehensive income for the three months ended September 30, 2010								494,922	(77)	494,845
				(11,992)				(11,992)		(11,992)

Cash dividends ($0.14 per share)										
Cumulative effect adjustments										
Noncontrolling interest										
Stock-based compensation		3,219	(356)					2,863		2,863
Balance, September 30, 2010	$ 44,388	$ 584,865	$ (26,101)	$ 2,366,276	$ 663,047	$ (16,718)	$ (44,365)	$ 3,571,392	$ (816)	$ 3,570,576

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,	
	2010	2009
	(Dollars In Thousands)	
Cash flows from operating activities		
Net income	$ 181,321	$ 140,477
Adjustments to reconcile net income to net cash provided by operating activities:		
Realized investment losses (gains)	46,886	71,331
Amortization of deferred policy acquisition costs and value of business acquired	146,761	250,837
Capitalization of deferred policy acquisition costs	(365,499)	(316,914)
Depreciation expense	7,184	5,928
Deferred income tax	(5,813)	(48,926)
Accrued income tax	112,281	25,077
Interest credited to universal life and investment products	658,488	749,552
Policy fees assessed on universal life and investment products	(471,383)	(441,410)
Change in reinsurance receivables	(230,423)	(81,583)
Change in accrued investment income and other receivables	(38,996)	(24,104)
Change in policy liabilities and other policyholders funds of traditional life and health products	328,042	170,502
Trading securities:		
Maturities and principal reductions of investments	262,153	446,993
Sale of investments	555,904	595,676
Cost of investments acquired	(769,120)	(587,057)
Other net change in trading securities	20,078	(152,691)
Change in other liabilities	23,478	(89,588)
Other, net	113,153	9,882
Net cash provided by operating activities	574,495	723,982
Cash flows from investing activities		
Maturities and principal reductions of investments, available-for-sale	1,372,385	2,003,690
Sale of investments, available-for-sale	2,807,438	1,250,831
Cost of investments acquired, available-for sale	(5,274,565)	(3,304,310)
Mortgage loans:		
New borrowings	(231,931)	(203,490)
Repayments	249,363	199,271
Change in investment real estate, net	(1,127)	(3,347)
Change in policy loans, net	27,062	22,531
Change in other long-term investments, net	(138,419)	(6,896)
Change in short-term investments, net	517,278	118,993
Net unsettled security transactions	80,412	48,742
Purchase of property and equipment	(7,050)	(5,989)
Net cash (used in) provided by investing activities	(599,154)	120,026
Cash flows from financing activities		
Borrowings under line of credit arrangements and long-term debt	116,000	212,000
Principal payments on line of credit arrangement and long-term debt	(275,000)	(122,000)
Issuance (repayment) of non-recourse funding obligations	(27,000)	
Dividends to shareowners	(34,257)	(27,069)
Issuance of common stock		132,575

Investments product deposits and change in universal life deposits		2,652,811		1,956,715
Investment product withdrawals		(2,459,566)		(2,902,277)
Other financing activities, net		(2,314)		(18,008)
Net cash used in financing activities		(29,326)		(768,064)
Change in cash		(53,985)		75,944
Cash at beginning of period		205,325		149,358
Cash at end of period	$	151,340	$	225,302

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 months period ended September 30, 2010, are not necessarily indicative of the results that may be expected for the year ending December 31, 2010. 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, 2009.

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, 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 became

Table of Contents

effective for the Company for the period ending March 31, 2010, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. This Update did not have a material impact on the Company s consolidated results of operations or financial position.

ASU No. 2009-16 Transfers and Servicing Accounting for Transfers of Financial Assets. In December of 2009, FASB issued ASU No. 2009-16 Transfers and Services Accounting for Transfers of Financial Assets. The amendments in this Update incorporate FASB Statement No. 166, *Accounting for Transfers of Financial Assets an amendment of SFAS No. 140* into the Accounting Standards Codification (ASC). That Statement was issued by the Board on June 12, 2009. This Update enhances the information that a reporting entity provides in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a continuing interest in transferred financial assets. This Update also eliminates the concept of a qualifying special-purpose entity (QSPE), changes the requirements for de-recognition of financial assets, and calls upon sellers of the assets to make additional disclosures. This Update is effective for interim or annual reporting periods beginning after November 15, 2009. This guidance was effective for the Company on January 1, 2010. As of January 1, 2010, the Company held interests in two previous transfers of financial assets to QSPEs, the 2007 Commercial Mortgage Securitization and the 1996 1999 Commercial Mortgage Securitization. As part of adoption of this guidance the Company reviewed these entities as part of our consolidation analysis of variable interest entities (VIEs). The conclusion of the review was that the former QSPEs should be consolidated by the Company. Please refer to Note 4, *Variable Interest Entities* for more information. The Company has not transferred any financial assets since the adoption of this standard. The Company will apply this guidance to all future transfers of financial assets.

ASU No. 2009-17 Consolidations Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities. In December of 2009, FASB issued ASU No. 2009-17 Consolidations Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities. The amendments to this Update incorporate FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)* (SFAS No. 167) into the ASC. SFAS No. 167 was issued by the Board on June 12, 2009. This Statement applies to all investments in VIEs beginning for the Company on January 1, 2010. This analysis will include QSPEs used for securitizations as SFAS No. 166 eliminated the concept of a QSPE which subjects former QSPEs to the provisions of FIN 46(R) as amended by this statement. Based on our review of our December 31, 2009 information, the impact of adoption of ASU No. 2009-17 (SFAS No. 167) resulted in the consolidation of two securitization trusts, the 2007 Commercial Mortgage Securitization and the 1996 1999 Commercial Mortgage Securitization. Please refer to Note 4, *Variable Interest Entities* for more information regarding the consolidation of these two trusts.

Accounting Pronouncements Not Yet Adopted

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 will be effective January 1, 2011. The Company is currently evaluating the impact of this Update.

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 and other disclosures related to the credit quality of the Company s mortgage loan portfolio. These new disclosure requirements will be effective for reporting periods ending on or after December 15, 2010. For the Company this will be December 31, 2010. This standard does not change current accounting for Financing Receivables and Loans, but only requires additional disclosures. The Company is evaluating the impact this Update will have on the footnotes to the financial statements.

Table of Contents

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 is currently evaluating the impact this Update will have on our financial position and results of operations.

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, 2009. There were no significant changes to the Company s accounting policies during the nine months ended September 30, 2010, except as noted above.

3. INVESTMENT OPERATIONS

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

	For The Three Months Ended September 30, 2010	For The Nine Months Ended September 30, 2010
	(Dollars In Thousands)	
Fixed maturities	$ 17,861	$ 30,237
Equity securities		13
Impairments on fixed maturity securities	(7,615)	(36,282)
Modco trading portfolio	96,689	204,749
Mortgage loans and other investments	(3,763)	(8,609)
	$ 103,172	$ 190,108

For the three and nine months ended September 30, 2010, gross realized gains on investments available-for-sale (fixed maturities, equity securities, and short-term investments) were $18.5 million and $61.8 million and gross realized losses were $8.1 million and $67.6 million, including $7.5 million and $36.0 million of impairment losses, respectively. The $7.5 million and $36.0 million exclude $0.1 million and $0.3 million of impairment losses in the trading portfolio for the three and nine months ended September 30, 2010, respectively.

For the three and nine months ended September 30, 2010, the Company sold securities in an unrealized gain position with a fair value (proceeds) of $652.4 million and $2.4 billion, respectively. The gains realized on the sale of these securities were $18.5 million and $61.8 million, respectively.

For the three and nine months ended September 30, 2010, the Company sold securities in an unrealized loss position with a fair value (proceeds) of $207.8 million and $442.0 million, respectively. The loss realized on the sale of these securities was $0.6 million and $31.6 million, respectively. The $31.6 million loss recognized on available-for-sale securities for the nine months ended September 30, 2010, includes $12.2 million of loss on the sale of certain oil industry holdings. The Company made the decision to sell these securities due to circumstances regarding the oil spill in the Gulf of Mexico. In addition, a $3.8 million loss was recognized on the sale of securities of which the issuer was a European financial institution. Also included in the $31.6 million loss is a $10.4 million loss due to the exchange of certain holdings as the issuer exited bankruptcy proceedings.

Table of Contents

The amortized cost and estimated fair value of the Company s investments classified as available-for-sale as of September 30, 2010, are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(Dollars In Thousands)			
2010				
Fixed maturities:				
Bonds				
Residential mortgage-backed securities	$ 3,019,820	$ 63,901	$ (193,082)	$ 2,890,639
Commercial mortgage-backed securities	165,073	9,447		174,520
Other asset-backed securities	867,648	1,625	(70,929)	798,344
U.S. government-related securities	1,187,000	75,160	(91)	1,262,069
Other government-related securities	195,446	8,074	(68)	203,452
States, municipals, and political subdivisions	751,248	54,082	(577)	804,753
Corporate bonds	14,280,879	1,426,469	(141,241)	15,566,107
	20,467,114	1,638,758	(405,988)	21,699,884
Equity securities	317,194	14,366	(8,739)	322,821
Short-term investments	412,166			412,166
	$ 21,196,474	$ 1,653,124	$ (414,727)	$ 22,434,871

As of September 30, 2010, the Company had an additional $3.1 billion of fixed maturities, $12.3 million of equity securities, and $71.5 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, 2010, 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	$ 482,217	$ 491,959
Due after one year through five years	3,776,610	3,883,575
Due after five years through ten years	5,858,895	6,365,726
Due after ten years	10,349,392	10,958,624
	$ 20,467,114	$ 21,699,884

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, commercial mortgage-backed securities, 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

Table of Contents

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 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, 2010, the Company recorded other-than-temporary impairments of investments of $12.9 million and $71.4 million, respectively. Of the $12.9 million of impairments for the three months ended September 30, 2010, $7.6 million was recorded in earnings and $5.3 million was recorded in other comprehensive income (loss). Of the $71.4 million of impairments for the nine months ended September 30, 2010, $36.3 million was recorded in earnings and $35.1 million was recorded in other comprehensive income (loss). For the three and nine months ended September 30, 2010, there were no other-than-temporary impairments related to equity securities. For the three and nine months ended September 30, 2010, there were $12.9 million and $71.4 million of other-than-temporary impairments related to debt securities, respectively. During these periods, 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.

The following chart is a rollforward of 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,**	
	2010	**2009**	**2010**	**2009**
	(Dollars In Thousands)			
Beginning balance	$ 31,576	$ 46,728	$ 25,076	$
Additions for newly impaired securities	6,211	11,601	25,661	67,019
Additions for previously impaired securities	1,179		2,930	7,136
Reductions for previously impaired securities due to a change in expected cash flows		(16,625)		(32,451)
Reductions for previously impaired securities that were sold in the current period	(2,947)	(17,949)	(17,648)	(17,949)
Ending balance	$ 36,019	$ 23,755	$ 36,019	$ 23,755

Table of Contents

The following table includes investments 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, 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	$ 102,086	$ (18,161)	$ 1,418,476	$ (174,921)	$ 1,520,562	$ (193,082)
Commercial mortgage-backed securities						
Other asset-backed securities	55,705	(1,791)	624,329	(69,138)	680,034	(70,929)
U.S. government-related securities	44,270	(91)			44,270	(91)
Other government-related securities	48,902	(58)	19,990	(10)	68,892	(68)
States, municipals, and political subdivisions	24,423	(577)			24,423	(577)
Corporate bonds	372,139	(25,063)	1,211,768	(116,178)	1,583,907	(141,241)
Equities	11,916	(3,833)	12,430	(4,906)	24,346	(8,739)
	$ 659,441	$ (49,574)	$ 3,286,993	$ (365,153)	$ 3,946,434	$ (414,727)

The residential mortgage-backed securities (RMBS) have a gross unrealized loss greater than twelve months of $174.9 million as of September 30, 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 corporate bonds category has gross unrealized losses greater than twelve months of $116.2 million as of September 30, 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 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 other asset-backed securities have a gross unrealized loss greater than twelve months of $69.1 million as of September 30, 2010. This category predominately includes student-loan backed auction rate securities whose underlying collateral is at least 97% guaranteed by the Federal Family Education Loan Program (FFELP). These losses relate to the auction rate securities (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 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, 2010, the Company had securities in its available-for-sale portfolio which were rated below investment grade of $3.0 billion and had an amortized cost of $3.3 billion. In addition, included in the Company s trading portfolio, the Company held $362.0 million of securities which were rated below investment grade. Approximately $563.1 million of the below investment grade securities were not publicly traded.

Table of Contents

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, 2010	For The Nine Months Ended September 30, 2010
	(Dollars In Thousands)	
Fixed maturities	$ 472,191	$ 1,059,929
Equity securities	13,970	6,986

4. VARIABLE INTEREST ENTITIES

In June of 2009, the FASB amended the guidance related to VIEs which was later codified in the ASC through ASU No. 2009-17. Among other accounting and disclosure requirements, this guidance replaces the quantitative-based risks and rewards calculation for determining which enterprise has a controlling financial interest in a VIE with an approach focused on identifying which enterprise has the power to direct the activities of a VIE that most significantly impact its economics and the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE. Additionally, the FASB amended the guidance related to accounting for transfers of financial assets which was later codified in the ASC through ASU No. 2009-16. This guidance, among other requirements, removed the concept of a QSPE used for the securitization of financial assets. Previously, QSPEs were excluded from the guidance related to VIEs. Upon adoption of ASU No. 2009-17 and ASU No. 2009-16 on January 1, 2010, the Company will no longer exclude QSPEs from the analysis of VIEs.

As part of adopting these updates, the Company updated its process for evaluating VIEs. The Company s analysis consists of a review of entities in which the Company has an ownership interest that is less than 100% (excluding debt and equity securities held as trading and available-for-sale), as well as entities with which the Company has significant contracts or other relationships that could possibly be considered variable interests. The Company reviews the characteristics of each of these applicable entities and compares those characteristics to the criteria of a VIE set forth in Topic 810 of the FASB ASC. If the entity is determined to be a VIE, the Company then performs a detailed review of all significant contracts and relationships (individually an interest , collectively interests) with the entity to determine whether the interest would be considered a variable interest under the guidance. The Company then performs a qualitative review of all variable interests with the entity and determines whether the Company: 1) has the power to direct the activities of the VIE that most significantly impact the VIE s economic performance and 2) the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the entity that could potentially be significant to the VIE.

Based on this analysis the Company had interests in two former QSPEs that were determined to be VIEs as of January 1, 2010. These two VIEs were trusts used to facilitate commercial mortgage loan securitizations. The determining factor was that the trusts had negligible or no equity at risk. The Company s variable interests in the trusts are created by the contract to service the mortgage loans held by the trusts as well as the retained beneficial interests in certain of these securities issued by the trusts. The activities that most significantly impact the economics of the trusts are predominantly related to the servicing of the mortgage loans, such as timely collection of principal and interest, direction of foreclosure proceedings, and management and sale of foreclosed real estate owned by the trusts. The Company is the servicer responsible for these activities and has the sole power to appoint such servicer through its beneficial interests in the securities. These criteria give the Company the power to direct the activities of the trusts that most significantly impact the trusts economic performance. Additionally, the Company is obligated, as an owner of the securities issued by the trusts, to absorb its share of losses on the securities. The Company s share of losses could potentially be significant to the trusts. Based on the fact that the Company has the power to direct the activities that most significantly impact the economics of the trusts and the obligation to absorb losses that could potentially be significant, it was determined that the Company is the primary beneficiary of the trusts, thus resulting in consolidation.

The assets of the trusts consist entirely of commercial mortgage loans and accrued interest, which are restricted and can only be used to satisfy the obligations of the trusts. The obligations of the trusts consist of commercial mortgage-backed certificates. The assets and obligations of the trusts are equal and thus, the trusts have no equity interest. The certificates are direct obligations of the trusts and are not guaranteed by the Company. The Company has no other obligations to the trusts other than those that are customary for a servicer of mortgage loans.

Table of Contents

Over the life of the trusts, the Company has not provided and will not provide any financial or other support to the trusts other than customary actions taken by a servicer of mortgage loans.

The following adjustments to the Company s consolidated condensed balance sheet were made as of January 1, 2010:

Adjustments to the Consolidated Condensed Balance Sheets

		As of January 1, 2010 (Dollars In Thousands)
Assets		
Fixed maturities:		
Commercial mortgage-backed securities at fair value (amortized cost - $873,196)	$	(844,535)(1)
Mortgage loans - securitized (net of loan loss reserve of $1.1 million)		1,018,000(2)
Total investments		173,465
Accrued investment income		361(2)
Total Assets	$	173,826
Liabilities		
Deferred income taxes	$	17,744(3)
Mortgage loan backed certificates		124,580(2)
Other liabilities		(1,400)(4)
Total liabilities		140,924
Shareowners equity		
Retained earnings		14,290(2)
Accumulated other comprehensive income (loss)		18,612(5)
Total shareowners equity		32,902
Total liabilities and shareowners equity	$	173,826

(1) The noncash portion for the consolidated condensed statements of cash flows for the three months ended March 31, 2010, was $873.2 million.

(2) The noncash portion for the consolidated condensed statements of cash flows for the three months ended March 31, 2010, is the amount presented.

(3) The noncash portion for the consolidated condensed statements of cash flows for the three months ended March 31, 2010, was $7.7 million.

(4) The other liabilities did not have an effect on the consolidated condensed statements of cash flows for the three months ended March 31, 2010.

(5) The accumulated other comprehensive income (loss) did not have an effect on the consolidated condensed statements of cash flows for the three months ended March 31, 2010.

The adjustments had a net zero impact to the consolidated condensed statements of cash flows.

The reduction in fixed maturity commercial mortgage-backed securities (CMBS) represents the beneficial interests held by the Company that have been removed due to the consolidation of the trusts. This amount is reflected in fixed maturities on the consolidated condensed balance sheet.

The increase in mortgage loans represents the mortgage loans held by the trusts that have been consolidated. This balance is net of a loan loss reserve of $1.1 million.

The increase in accrued investment income is the result of accruing interest on the entire pool of mortgage loans.

The increase in deferred income taxes is a result of a change in temporary tax differences arising from the adjustments to shareowners equity.

The mortgage loan backed certificates liability represents the commercial mortgage-backed securities issued by the trusts and held by third parties.

The decrease in other liabilities is a decrease in amounts payable to the trusts of approximately $1.4 million. Upon consolidation of the trusts as of January 1, 2010, the Company adjusted retained earnings to reflect after tax interest income not recognized in prior periods due to the securitization of the commercial mortgage loans. If the Company had held the mortgage loans as opposed to the retained beneficial interest securities, the Company s retained earnings would have been $14.3 million higher over the life of the securities.

Table of Contents

The adjustment to accumulated other comprehensive income (loss) was a result of different accounting basis for mortgage loans and the CMBS. As of December 31, 2009, the retained beneficial interest securities were carried at fair value in the balance sheet and had an after tax unrealized loss in accumulated other comprehensive income (loss) of $18.6 million. Upon consolidation of the trusts on January 1, 2010, the Company consolidated the mortgage loans held by the trusts which are carried at amortized cost less any related loan loss reserve. The retained beneficial interest securities as well as the associated unrealized loss were eliminated in consolidation.

5. GOODWILL

During the nine months ended September 30, 2010, 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 2010 on the portion of tax goodwill in excess of GAAP basis goodwill. As of September 30, 2010, the Company had an aggregate goodwill balance of $115.5 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 compared 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 its operating segments (which are 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 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, 2009, 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 September 30, 2010 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, the decline in market capitalization 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.

Table of Contents

6. DEBT AND OTHER OBLIGATIONS

Non-recourse funding obligations outstanding as of September 30, 2010, 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	$	548,000	2052	1.49%

Golden Gate II Captive Insurance Company (Golden Gate II), a special purpose financial captive insurance company wholly owned by Protective Life Insurance Company (PLICO), had $575 million of outstanding non-recourse funding obligations as of September 30, 2010. Of this amount, $548.0 million were owned by external parties and $27.0 million were owned by affiliates.

7. COMMITMENTS AND CONTINGENCIES

The Company has entered into indemnity agreements with each of its current directors that provides, 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. The Company does not believe such assessments will be materially different from amounts already provided for in the financial statements. Most of these laws do provide, however, that an assessment may be excused or deferred if it would threaten an insurer s own financial strength.

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. The Company, in the ordinary course of business, is involved in such litigation and arbitration. The occurrence of such litigation and arbitration may become more frequent and/or severe when general economic conditions have deteriorated. Although the Company cannot predict the outcome of any such litigation or arbitration, the Company does not believe that any such outcome will have a material impact on its financial condition or results of the operations.

17

Table of Contents

8. 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, 2010	For The Three Months Ended September 30, 2009	For The Nine Months Ended September 30, 2010	For The Nine Months Ended September 30, 2009
	(Dollars In Thousands)			
Net income	$ 70,371	$ 27,585	$ 181,321	$ 140,477
Change in net unrealized gains (losses) on investments, net of income tax: (three months: 2010 - $211,169; 2009 - $342,694; nine months: 2010 - $484,424; 2009 - $655,781)	392,180	626,065	898,995	1,192,473
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: 2010 - $19,461; 2009 - $5,633; nine months: 2010 - $9,006; 2009 - $(6,755))	36,141	10,462	16,725	(12,544)
Change in accumulated (loss) gain - derivatives, net of income tax: (three months: 2010 - $1,951; 2009 - $1,833; nine months: 2010 - $2,145; 2009 - $12,154)	3,581	3,299	3,347	21,877
Minimum pension liability adjustment, net of income tax: (three months: 2010 - $325; 2009 - $178; nine months: 2010 - $974; 2009 - $533)	603	329	1,808	989
Reclassification adjustment for investment amounts included in net income, net of income tax: (three months: 2010 - $(3,583); 2009 - $9,367; nine months: 2010 - $2,036; 2009 - $48,890)	(6,663)	17,290	3,996	89,443
Reclassification adjustment for derivative amounts included in net income, net of income tax: (three months: 2010 - $(760); 2009 - $(666); nine months: 2010 - $(966); 2009 - $(363))	(1,368)	(1,198)	(1,738)	(654)
Comprehensive income (loss)	494,845	683,832	1,104,454	1,432,061
Comprehensive income (loss) attributable to noncontrolling interests	77		277	
Comprehensive income (loss) attributable to Protective Life Corporation	$ 494,922	$ 683,832	$ 1,104,731	$ 1,432,061

9. STOCK-BASED COMPENSATION

The criteria for payment of performance awards is based primarily upon a comparison of the Company s average return on average equity over a four-year period (earlier upon the death, disability, or retirement of the executive, or in certain circumstances, upon a change in control of the Company) to that of a comparison group of publicly held life and multi-line insurance companies. For the 2008 awards, if the Company s results are below the 25th percentile of the comparison group, no portion of the award is earned. For the 2005-2007 awards, if the Company s results are below the 40th percentile of the comparison group, no portion of the award is earned. If the Company s results are at or above the 90th percentile, the award maximum is earned. Awards are paid in shares of the Company s Common Stock. There were no performance share awards issued during the nine months ended September 30, 2010 or 2009.

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 grants 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, 2009	$ 22.28	2,469,202
SARs granted	18.34	344,400
SARs exercised / forfeited / expired	21.11	(457,404)
Balance as of September 30, 2010	$ 21.93	2,356,198

The SARs issued for the nine months ended September 30, 2010, had estimated fair values at grant date of $3.3 million. These fair values were estimated using a Black-Scholes option pricing model. The assumptions used in

Table of Contents

this pricing model varied depending on the vesting period of awards. Assumptions used in the model for the 2010 SARs granted (the simplified method under the ASC Compensation-Stock Compensation Topic was used for the 2010 awards) were as follows: an expected volatility of 69.4%, a risk-free interest rate of 2.6%, a dividend rate of 2.4%, a zero percent forfeiture rate, and an expected exercise date of 2016. 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.

Additionally, the Company issued 360,450 restricted stock units for the nine months ended September 30, 2010. These awards had a total fair value at grant date of $6.6 million. Approximately half of these restricted stock units vest in 2013, and the remainder vest in 2014.

10. EMPLOYEE BENEFIT PLANS

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

	For The Three Months Ended September 30,		For The Nine Months Ended September 30,	
	2010	2009	2010	2009
	(Dollars In Thousands)			
Service cost benefits earned during the period	$ 2,068	$ 1,889	$ 6,204	$ 5,667
Interest cost on projected benefit obligation	2,357	2,395	7,071	7,185
Expected return on plan assets	(2,312)	(2,531)	(6,936)	(7,593)
Amortization of prior service cost	(98)	(98)	(294)	(294)
Amortization of actuarial losses	1,026	568	3,078	1,704
Total benefit cost	$ 3,041	$ 2,223	$ 9,123	$ 6,669

During the nine months ended September 30, 2010, the Company made a $6.5 million contribution to its defined benefit pension plan for the 2009 plan year and a $0.2 million contribution to its defined benefit pension plan for the 2010 plan year. In addition, during October of 2010, the Company contributed $1.6 million to the defined benefit pension plan for the 2010 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 percentage 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, 2010, was immaterial to the Company s financial statements.

Table of Contents

11. 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.

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,	
	2010	2009	2010	2009
	(Dollars In Thousands, Except Per Share Amounts)			
Calculation of basic earnings per share:				
Net income available to PLC s common shareowners	$ 70,448	$ 27,585	$ 181,598	$ 140,477
Average shares issued and outstanding	85,662,988	85,579,525	85,628,404	77,557,599
Issuable under various deferred compensation plans	940,581	901,715	927,357	908,086
Weighted shares outstanding - Basic	86,603,569	86,481,240	86,555,761	78,465,685
Per share:				
Net income available to PLC s common shareowners - basic	$ 0.81	$ 0.32	$ 2.10	$ 1.79
Calculation of diluted earnings per share:				
Net income available to PLC s common shareowners	$ 70,448	$ 27,585	$ 181,598	$ 140,477
Weighted shares outstanding - Basic	86,603,569	86,481,240	86,555,761	78,465,685
Stock appreciation rights (SARs)(1)	468,886	446,269	466,511	332,604
Issuable under various other stock-based compensation plans	110,102	111,244	134,299	136,784
Restricted stock units	519,035	333,906	483,650	221,232
Weighted shares outstanding - Diluted	87,701,592	87,372,659	87,640,221	79,156,305
Per share:				
Net income available to PLC s common shareowners - diluted	$ 0.80	$ 0.32	$ 2.07	$ 1.77

(1) Excludes 1,475,645 and 1,558,373 as of September 30, 2010 and 2009, 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.

12. INCOME TAXES

During the three months ended September 30, 2010, earnings were impacted favorably by $0.7 million due to the release of an unrecognized income tax benefit liability that related to a compensation-related tax issue. The measurement of the unrecognized tax benefit was recently reassessed due to recent developments related to the issue, and the Company now believes that the full amount of the tax benefit has a greater than 50% chance of being fully realized. During the nine months ended September 30, 2010, earnings were impacted favorably by $3.3 million due to the aforementioned issue, the release of an unrecognized income tax benefit liability that related to a tax-basis policy liability issue, and the closing of the 2005 tax year s statute of limitations. The Company reassessed the tax-basis policy liability issue due to recent technical guidance that confirmed the Company s historical calculations. 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, 2010, based upon its estimate of its annual 2010 income. For the three and nine months ended September 30, 2009, due to the unpredictability at that time of future investment losses and certain elements of operating income, the Company was not able to reasonably estimate an expected annual effective tax rate. Instead, the Company computed an effective income tax rate based upon year-to-date reported income. The effective tax rate for the three

Table of Contents

and nine months ended September 30, 2010, was 34.2% and 33.5%, respectively, and 33.7% and 34.4% for the three and nine months ended September 30, 2009, 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, 2010.

13. FAIR VALUE OF FINANCIAL INSTRUMENTS

Effective January 1, 2008, 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. In the first quarter of 2009, the Company 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 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, 2010:

	Level 1	Level 2	Level 3	Total
		(Dollars In Thousands)		
Assets:				
Fixed maturity securities - available-for-sale				
Residential mortgage-backed securities	$	$ 2,890,619	$ 20	$ 2,890,639
Commercial mortgage-backed securities		154,354	20,166	174,520
Other asset-backed securities		196,125	602,219	798,344
U.S. government-related securities	974,455	272,491	15,123	1,262,069
States, municipals, and political subdivisions		804,671	82	804,753
Other government-related securities	14,993	188,459		203,452
Corporate bonds	100	15,425,707	140,300	15,566,107
Total fixed maturity securities - available-for-sale	989,548	19,932,426	777,910	21,699,884
Fixed maturity securities - trading				
Residential mortgage-backed securities		472,360		472,360
Commercial mortgage-backed securities		137,632		137,632
Other asset-backed securities		16,131	62,756	78,887
U.S. government-related securities	409,105	43,661	3,686	456,452
States, municipals, and political subdivisions		145,286		145,286
Other government-related securities		158,567		158,567
Corporate bonds		1,685,026	4,532	1,689,558
Total fixed maturity securities - trading	409,105	2,658,663	70,974	3,138,742
Total fixed maturity securities	1,398,653	22,591,089	848,884	24,838,626
Equity securities	234,234	19,399	81,518	335,151
Other long-term investments (1)	1,459	340	11,318	13,117
Short-term investments	475,375	8,323		483,698
Total investments	2,109,721	22,619,151	941,720	25,670,592
Cash	151,340			151,340
Other assets	5,633			5,633
Assets related to separate accounts				
Variable annuity	3,899,308			3,899,308
Variable universal life	336,299			336,299
Total assets measured at fair value on a recurring basis	$ 6,502,301	$ 22,619,151	$ 941,720	$ 30,063,172
Liabilities:				
Annuity account balances (2)	$	$	$ 144,166	$ 144,166
Other liabilities (1)	14,031	40,101	339,581	393,713
Total liabilities measured at fair value on a recurring basis	$ 14,031	$ 40,101	$ 483,747	$ 537,879

(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, 2009:

	Level 1	Level 2	Level 3	Total
		(Dollars In Thousands)		
Assets:				
Fixed maturity securities - available-for-sale				
Residential mortgage-backed securities	$	$ 3,370,688	$ 23	$ 3,370,711
Commercial mortgage-backed securities		143,486	844,535	988,021
Other asset-backed securities		360,797	693,930	1,054,727
U.S. government-related securities	444,302	30,198	15,102	489,602
States, municipals, and political subdivisions		350,632	86	350,718
Other government-related securities	16,992	389,379		406,371
Corporate bonds	200	13,127,347	86,328	13,213,875
Total fixed maturity securities - available-for-sale	461,494	17,772,527	1,640,004	19,874,025
Fixed maturity securities - trading	277,108	2,574,205	105,089	2,956,402
Total fixed maturity securities	738,602	20,346,732	1,745,093	22,830,427
Equity securities	204,697	92	70,708	275,497
Other long-term investments (1)		22,926	16,525	39,451
Short-term investments	983,123	66,486		1,049,609
Total investments	1,926,422	20,436,236	1,832,326	24,194,984
Cash	205,325			205,325
Other assets	4,977			4,977
Assets related to separate accounts				
Variable annuity	2,948,457			2,948,457
Variable universal life	316,007			316,007
Total assets measured at fair value on a recurring basis	$ 5,401,188	$ 20,436,236	$ 1,832,326	$ 27,669,750
Liabilities:				
Annuity account balances (2)	$	$	$ 149,893	$ 149,893
Other liabilities (1)		43,045	105,838	148,883
Total liabilities measured at fair value on a recurring basis	$	$ 43,045	$ 255,731	$ 298,776

(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.

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, 2010.

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 ABS). As of September 30, 2010, the Company held $3.9 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, 2010, the Company held $685.2 million of Level 3 ABS, which included $62.8 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. The model uses the discount margin and projected average life of comparable actively traded FFELP student loan-backed floating-rate asset-backed securities, along with a discount related to the current illiquidity of the ARS. These comparable securities are selected based on their underlying assets (i.e. FFELP-backed student loans) and vintage. As a result of the ARS market collapse during 2008, the Company prices its ARS using an internally developed model which utilizes a market based approach to valuation. 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.

Available-for-sale ABSs classified as Level 3 had, but were not limited to, the following inputs:

Investment grade credit rating	100%
Weighted-average yield	1.5%
Amortized cost	$672.7 million
Weighted-average life	2.8 years

Corporate bonds, U.S. Government-related securities, and Other government related securities

As of September 30, 2010, the Company classified approximately $18.7 billion of corporate bonds, U.S. government-related securities, 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 utilizes 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, 2010, the Company classified approximately $163.7 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, 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.

Table of Contents

Bonds and securities classified as Level 3 used security specific inputs that included, but were not limited to, the following:

Investment grade credit rating	89.9%
Weighted-average market yield	4.6%
Weighted-average coupon	6.3%
Amortized cost	$149.5 million
Weighted-average stated maturity	6.5 years

Equities

As of September 30, 2010, the Company held approximately $100.9 million of equity securities classified as Level 2 and Level 3. Of this total, $60.7 million represents Federal Home Loan Bank stock. The Company believes that the cost of the Federal Home Loan Bank 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 14, *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, 2010, 78.2% 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 analysis.

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

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

Derivative instruments classified as Level 3 were total return swaps and 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 benefit (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 14 *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 1,000 risk neutral 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.

Table of Contents

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.

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 on a stochastic basis using 1,000 risk neutral 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.

Included in the chart below, are current key assumptions which include risk margins for the Company. These assumptions are reviewed for reasonableness on a quarterly basis.

Asset Earned Rate	5.90%
Admin Expense per Policy	$91
Partial Withdrawal Rate (for ages less than 70)	2.20%
Partial Withdrawal Rate (for ages 70 and greater)	2.20%
Mortality	65% of 94 GMDB table
Lapse	2% to 50% 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, 2010, ranged from a one month rate of 0.84%, a 5 year rate of 2.98%, and a 30 year rate of 4.84%.

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, 2010, for which the Company has used significant unobservable inputs (Level 3):

	Beginning Balance	Total Realized and Unrealized Gains (losses): Included in Earnings	Total Realized and Unrealized Gains (losses): 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.

For the three months ended September 30, 2010, $55.6 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, 2010.

For the three months ended September 30, 2010, $59.4 million of securities were transferred out of Level 3. This amount was transferred 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 by independent pricing services or brokers, utilizing no significant unobservable inputs, as of September 30, 2010.

For the three months ended September 30, 2010, there were no transfers between Level 1 and 2.

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, 2009, for which the Company has used significant unobservable inputs (Level 3):

		Total Realized and Unrealized Gains (losses)					Total Gains (losses) included in Earnings related to Instruments still held at the Reporting Date
	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	
	(Dollars In Thousands)						
Assets:							
Fixed maturity securities - available-for-sale							
Residential mortgage-backed securities	$ 30	$ (13,987)	$ 9,418	$ 1,012	$ 3,555	$ 28	$
Commercial mortgage-backed securities	817,585		35,205	(28,990)		823,800	
Other asset-backed securities	724,186		9,985	10,147	(3,477)	740,841	
U.S. government-related securities	15,060		1,634	(97)	(1,375)	15,222	
States, municipals, and political subdivisions	89					89	
Other government-related securities							
Corporate bonds	69,517		6,369	18,898	11,103	105,887	
Total fixed maturity securities - available-for-sale	1,626,467	(13,987)	62,611	970	9,806	1,685,867	
Fixed maturity securities - trading	86,355	4,808		(449)	(1,355)	89,359	3,393
Total fixed maturity securities	1,712,822	(9,179)	62,611	521	8,451	1,775,226	3,393
Equity securities	69,384		14	1,251	(21)	70,628	
Other long-term investments (1)	156,386	(114,133)				42,253	(114,133)
Short-term investments	664				(664)		
Total investments	1,939,256	(123,312)	62,625	1,772	7,766	1,888,107	(110,740)
Total assets measured at fair value on a recurring basis	$ 1,939,256	$ (123,312)	$ 62,625	$ 1,772	$ 7,766	$ 1,888,107	$ (110,740)
Liabilities:							
Annuity account balances (2)	$ 152,427	$ (1,992)	$	$ 4,348	$	$ 150,071	$
Other liabilities (1)	66,131	(75,648)				141,779	(75,648)
Total liabilities measured at fair value on a recurring basis	$ 218,558	$ (77,640)	$	$ 4,348	$	$ 291,850	$ (75,648)

(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, 2010, for which the Company has used significant unobservable inputs (Level 3):

	Beginning Balance	Total Realized and Unrealized Gains (losses) 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. See Note 4, *Variable Interest Entities*.

For the nine months ended September 30, 2010, $55.8 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, 2010.

For the nine months ended September 30, 2010, $147.3 million of securities were transferred out of Level 3. This amount was transferred 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, 2010.

For the nine months ended September 30, 2010, there were no transfers between Level 1 and 2.

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, 2009, for which the Company has used significant unobservable inputs (Level 3):

	Beginning Balance	Total Realized and Unrealized Gains (losses) Included in Earnings	Total Realized and Unrealized Gains (losses) 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	$ 34	$ (13,987)	$ 9,417	$ 1,009	$ 3,555	$ 28	$
Commercial mortgage-backed securities	855,817		12,768	(44,785)		823,800	
Other asset-backed securities	682,710	(31)	51,957	9,682	(3,477)	740,841	
U.S. government-related securities	10,072		933	14,768	(10,551)	15,222	
States, municipals, and political subdivisions	93			(4)		89	
Other government-related securities							
Corporate bonds	78,770	(49)	6,194	(11,574)	32,546	105,887	
Total fixed maturity securities - available-for-sale	1,627,496	(14,067)	81,269	(30,904)	22,073	1,685,867	
Fixed maturity securities - trading	32,645	8,345		75,044	(26,675)	89,359	6,496
Total fixed maturity securities	1,660,141	(5,722)	81,269	44,140	(4,602)	1,775,226	6,496
Equity securities	76,411		580	(6,342)	(21)	70,628	
Other long-term investments (1)	256,973	(214,720)				42,253	(214,720)
Short-term investments	1,161		(286)		(875)		
Total investments	1,994,686	(220,442)	81,563	37,798	(5,498)	1,888,107	(208,224)
Total assets measured at fair value on a recurring basis	$ 1,994,686	$ (220,442)	$ 81,563	$ 37,798	$ (5,498)	$ 1,888,107	$ (208,224)
Liabilities:							
Annuity account balances (2)	$ 152,762	$ (3,261)	$	$ 5,952	$	$ 150,071	$
Other liabilities (1)	113,311	(28,468)				141,779	(28,468)
Total liabilities measured at fair value on a recurring basis	$ 266,073	$ (31,729)	$	$ 5,952	$	$ 291,850	$ (28,468)

(1) Represents certain freestanding and embedded derivatives.
(2) Represents liabilities related to equity indexed annuities.

Total realized and unrealized gains (losses) on Level 3 assets and liabilities are primarily reported in either realized investment gains (losses) within the consolidated condensed statements of income 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, 2010		December 31, 2009	
	Carrying Amounts	Fair Values	Carrying Amounts	Fair Values
	(Dollars In Thousands)			
Assets:				
Mortgage loans on real estate	$ 4,884,102	$ 5,550,397	$ 3,883,414	$ 4,130,285
Policy loans	767,214	767,214	794,276	794,276
Liabilities:				
Stable value product account balances	$ 3,105,822	$ 3,363,073	$ 3,581,150	$ 3,758,422
Annuity account balances	10,451,322	10,208,697		