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**DELAWARE**

(State or other jurisdiction of incorporation or organization)

**95-2492236**

(IRS Employer Identification Number)

**2801 HIGHWAY 280 SOUTH**

**BIRMINGHAM, ALABAMA 35223**

(Address of principal executive offices and zip code)

Registrant's telephone number, including area code **(205) 268-1000**

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  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Accelerated Filer

Non-accelerated filer

Smaller Reporting Company

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

Number of shares of Common Stock, \$0.50 Par Value, outstanding as of July 23, 2014: 78,861,427

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**PROTECTIVE LIFE CORPORATION**  
**QUARTERLY REPORT ON FORM 10-Q**  
**FOR QUARTERLY PERIOD ENDED JUNE 30, 2014**

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## PROTECTIVE LIFE CORPORATION

## CONSOLIDATED CONDENSED STATEMENTS OF INCOME

(Unaudited)

|  | For The<br>Three Months Ended<br>June 30, |            | For The<br>Six Months Ended<br>June 30, |              |
|--|---|------------|---|--------------|
|  | 2014                                      | 2013       | 2014                                    | 2013         |
| (Dollars In Thousands, Except Per Share Amounts)   |   |            |   |              |
| <b>Revenues</b>  |   |            |   |              |
| Premiums and policy fees   | \$ 851,802                                | \$ 756,331 | \$ 1,667,698                            | \$ 1,483,178 |
| Reinsurance ceded  | (342,968)                                 | (390,490)  | (670,681)                               | (725,840)    |
| Net of reinsurance ceded   | 508,834                                   | 365,841    | 997,017                                 | 757,338      |
| Net investment income  | 550,816                                   | 466,220    | 1,088,979                               | 923,854      |
| Realized investment gains (losses):  |   |            |   |              |
| Derivative financial instruments   | (89,926)                                  | 143,881    | (195,276)                               | 151,266      |
| All other investments  | 80,148                                    | (109,978)  | 152,262                                 | (114,123)    |
| Other-than-temporary impairment losses   | (461)                                     | (1,789)    | (884)                                   | (3,129)      |
| Portion recognized in other comprehensive income (before taxes)  | (999)                                     | (2,211)    | (2,167)                                 | (5,455)      |
| Net impairment losses recognized in earnings   | (1,460)                                   | (4,000)    | (3,051)                                 | (8,584)      |
| Other income   | 106,931                                   | 94,392     | 205,970                                 | 179,419      |
| Total revenues   | 1,155,343                                 | 956,356    | 2,245,901                               | 1,889,170    |
| <b>Benefits and expenses</b>   |   |            |   |              |
| Benefits and settlement expenses, net of reinsurance ceded: (three months: 2014 - \$328,555; 2013 - \$370,752; six months: 2014 - \$633,387; 2013 - \$678,058) | 747,816                                   | 557,866    | 1,476,335                               | 1,139,746    |
| Amortization of deferred policy acquisition costs and value of business acquired   | 51,531                                    | 74,946     | 107,113                                 | 127,185      |
| Other operating expenses, net of reinsurance ceded: (three months: 2014 - \$46,545; 2013 - \$50,406; six months: 2014 - \$90,311; 2013 - \$91,395)             | 193,786                                   | 166,531    | 375,038                                 | 347,599      |
| Total benefits and expenses  | 993,133                                   | 799,343    | 1,958,486                               | 1,614,530    |
| <b>Income before income tax</b>  | 162,210                                   | 157,013    | 287,415                                 | 274,640      |
| Income tax expense   | 54,233                                    | 53,814     | 95,799                                  | 93,150       |
| <b>Net income</b>  | \$ 107,977                                | \$ 103,199 | \$ 191,616                              | \$ 181,490   |
| Net income - basic   | \$ 1.35                                   | \$ 1.30    | \$ 2.40                                 | \$ 2.29      |
| Net income - diluted   | \$ 1.33                                   | \$ 1.27    | \$ 2.36                                 | \$ 2.24      |
| Cash dividends paid per share  | \$ 0.24                                   | \$ 0.20    | \$ 0.44                                 | \$ 0.38      |
| Average shares outstanding - basic   | 79,979,153                                | 79,404,770 | 79,794,831                              | 79,272,814   |
| Average shares outstanding - diluted   | 81,446,277                                | 81,087,238 | 81,160,800                              | 80,898,042   |

See Notes to Consolidated Condensed Financial Statements



Table of Contents**PROTECTIVE LIFE CORPORATION****CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**

(Unaudited)

|  | For The<br>Three Months Ended<br>June 30, |                     | For The<br>Six Months Ended<br>June 30, |                     |
|--|---|---------------------|---|---------------------|
|  | 2014                                      | 2013                | 2014                                    | 2013                |
|  | (Dollars In Thousands)                    |                     |   |                     |
| <b>Net income</b>  | \$ 107,977                                | \$ 103,199          | \$ 191,616                              | \$ 181,490          |
| Other comprehensive income (loss):   |   |                     |   |                     |
| Change in net unrealized gains (losses) on investments, net of income tax: (three months: 2014 - \$216,476; 2013 - \$(420,013); six months: 2014 - \$476,065; 2013 - \$(496,308))  | 402,027                                   | (780,022)           | 884,120                                 | (921,713)           |
| Reclassification adjustment for investment amounts included in net income, net of income tax: (three months: 2014 - \$(6,558); 2013 - \$(6,131); six months: 2014 - \$(8,581); 2013 - \$(8,835))   | (12,180)                                  | (11,387)            | (15,936)                                | (16,409)            |
| 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: 2014 - \$(571); 2013 - \$(1,293); six months: 2014 - \$1,858; 2013 - \$2,926) | (1,061)                                   | (2,402)             | 3,450                                   | 5,435               |
| Change in accumulated (loss) gain - derivatives, net of income tax: (three months: 2014 - \$(325); 2013 - \$(1,606); six months: 2014 - \$(9); 2013 - \$(63))  | (604)                                     | (2,983)             | (17)                                    | (117)               |
| Reclassification adjustment for derivative amounts included in net income, net of income tax: (three months: 2014 - \$214; 2013 - \$203; six months: 2014 - \$449; 2013 - \$377)   | 399                                       | 377                 | 835                                     | 700                 |
| Change in postretirement benefits liability adjustment, net of income tax: (three months: 2014 - \$1,896; 2013 - \$(922); six months: 2014 - \$1,264; 2013 - \$(1,844))  | 3,520                                     | (1,712)             | 2,347                                   | (3,424)             |
| <b>Total other comprehensive income (loss)</b>   | <b>392,101</b>                            | <b>(798,129)</b>    | <b>874,799</b>                          | <b>(935,528)</b>    |
| <b>Total comprehensive income (loss)</b>   | <b>\$ 500,078</b>                         | <b>\$ (694,930)</b> | <b>\$ 1,066,415</b>                     | <b>\$ (754,038)</b> |

See Notes to Consolidated Condensed Financial Statements

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**PROTECTIVE LIFE CORPORATION**  
**CONSOLIDATED CONDENSED BALANCE SHEETS**

(Unaudited)

|   | June 30, 2014          | As of     | December 31, 2013 |
|---|------------------------|-----------|-------------------|
|   | (Dollars In Thousands) |           |                   |
| <b>Assets</b>   |                        |           |                   |
| Fixed maturities, at fair value (amortized cost: 2014 - \$34,244,088; 2013 - \$33,662,295)                    | \$ 37,164,427          | \$        | 34,815,931        |
| Fixed maturities, at amortized cost (fair value: 2014 - \$451,382; 2013 - \$335,676)                          | 400,000                |           | 365,000           |
| Equity securities, at fair value (cost: 2014 - \$771,004; 2013 - \$675,758)                                   | 792,047                |           | 646,027           |
| Mortgage loans (2014 and 2013 includes: \$531,141 and \$627,731 related to securitizations)                   | 5,294,729              |           | 5,493,492         |
| Investment real estate, net of accumulated depreciation (2014 - \$1,123; 2013 - \$1,066)                      | 18,856                 |           | 20,413            |
| Policy loans  | 1,778,379              |           | 1,815,744         |
| Other long-term investments   | 475,719                |           | 521,811           |
| Short-term investments  | 208,624                |           | 134,146           |
| Total investments   | 46,132,781             |           | 43,812,564        |
| Cash  | 361,088                |           | 466,542           |
| Accrued investment income   | 485,620                |           | 465,333           |
| Accounts and premiums receivable, net of allowance for uncollectible amounts (2014 - \$4,322; 2013 - \$4,283) | 101,891                |           | 101,039           |
| Reinsurance receivables   | 6,132,712              |           | 6,175,115         |
| Deferred policy acquisition costs and value of business acquired  | 3,273,275              |           | 3,570,215         |
| Goodwill  | 103,914                |           | 105,463           |
| Property and equipment, net of accumulated depreciation (2014 - \$115,056; 2013 - \$111,579)                  | 53,421                 |           | 52,403            |
| Other assets  | 385,060                |           | 432,151           |
| Assets related to separate accounts   |                        |           |                   |
| Variable annuity  | 13,304,455             |           | 12,791,438        |
| Variable universal life   | 823,747                |           | 783,618           |
| <b>Total assets</b>   | <b>\$ 71,157,964</b>   | <b>\$</b> | <b>68,755,881</b> |

See Notes to Consolidated Condensed Financial Statements

Table of Contents**PROTECTIVE LIFE CORPORATION****CONSOLIDATED CONDENSED BALANCE SHEETS**

(continued)

(Unaudited)

|  | June 30, 2014          | As of     | December 31, 2013 |
|--|------------------------|-----------|-------------------|
|  | (Dollars In Thousands) |           |                   |
| <b>Liabilities</b>   |                        |           |                   |
| Future policy benefits and claims  | \$ 29,823,111          | \$        | 29,772,325        |
| Unearned premiums  | 1,586,785              |           | 1,549,815         |
| Total policy liabilities and accruals  | 31,409,896             |           | 31,322,140        |
| Stable value product account balances  | 2,435,995              |           | 2,559,552         |
| Annuity account balances   | 11,071,468             |           | 11,125,253        |
| Other policyholders funds  | 1,400,817              |           | 1,214,380         |
| Other liabilities  | 1,381,570              |           | 1,143,371         |
| Income tax payable   | 99,869                 |           | 12,761            |
| Deferred income taxes  | 1,489,331              |           | 1,050,533         |
| Non-recourse funding obligations   | 579,078                |           | 562,448           |
| Repurchase program borrowings  | 420,490                |           | 350,000           |
| Debt   | 1,445,000              |           | 1,585,000         |
| Subordinated debt securities   | 540,593                |           | 540,593           |
| Liabilities related to separate accounts   |                        |           |                   |
| Variable annuity   | 13,304,455             |           | 12,791,438        |
| Variable universal life  | 823,747                |           | 783,618           |
| Total liabilities  | 66,402,309             |           | 65,041,087        |
| <b>Commitments and contingencies - Note 10</b>   |                        |           |                   |
| <b>Shareowners equity</b>  |                        |           |                   |
| Preferred Stock; \$1 par value, shares authorized: 4,000,000; Issued: None   |                        |           |                   |
| Common Stock, \$.50 par value, shares authorized: 2014 and 2013 - 160,000,000 shares issued: 2014 and 2013 - 88,776,960  | \$ 44,388              | \$        | 44,388            |
| Additional paid-in-capital   | 610,451                |           | 606,934           |
| Treasury stock, at cost (2014 - 9,915,533; 2013 - 10,199,514)  | (194,838)              |           | (200,416)         |
| Retained earnings  | 2,926,789              |           | 2,769,822         |
| Accumulated other comprehensive income (loss):   |                        |           |                   |
| Net unrealized gains (losses) on investments, net of income tax: (2014 - \$757,392; 2013 - \$289,908)  | 1,406,584              |           | 538,400           |
| Net unrealized (losses) gains relating to other-than-temporary impaired investments for which a portion has been recognized in earnings, net of income tax: (2014 - \$2,183; 2013 - \$325) | 4,053                  |           | 603               |
| Accumulated loss - derivatives, net of income tax: (2014 - \$(226); 2013 - \$(666))  | (417)                  |           | (1,235)           |
| Postretirement benefits liability adjustment, net of income tax: (2014 - \$(22,268); 2013 - \$(23,532))  | (41,355)               |           | (43,702)          |
| Total shareowners equity   | 4,755,655              |           | 3,714,794         |
| <b>Total liabilities and shareowners equity</b>  | <b>\$ 71,157,964</b>   | <b>\$</b> | <b>68,755,881</b> |

See Notes to Consolidated Condensed Financial Statements





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(Unaudited)

|   | <b>Common<br/>Stock</b> | <b>Additional<br/>Paid-In-<br/>Capital</b> | <b>Treasury<br/>Stock</b> | <b>Retained<br/>Earnings</b> | <b>Accumulated<br/>Other<br/>Comprehensive<br/>Income</b> | <b>Total<br/>Shareowners<br/>equity</b> |
|---|-------------------------|--|---------------------------|------------------------------|---|---|
|   | (Dollars In Thousands)  |  |                           |                              |   |   |
| Balance, December 31, 2013  | \$ 44,388               | \$ 606,934                                 | \$ (200,416)              | \$ 2,769,822                 | \$ 494,066  | \$ 3,714,794                            |
| Net income for the six<br>months ended June 30, 2014              |                         |  |                           | 191,616                      |   | 191,616                                 |
| Other comprehensive income  |                         |  |                           |                              | 874,799   | 874,799                                 |
| Comprehensive income for<br>the six months ended<br>June 30, 2014 |                         |  |                           |                              |   | 1,066,415                               |
| Cash dividends (\$0.440 per<br>share)                             |                         |  |                           | (34,649)                     |   | (34,649)                                |
| Stock-based compensation  |                         | 3,517                                      | 5,578                     |                              |   | 9,095                                   |
| Balance, June 30, 2014  | \$ 44,388               | \$ 610,451                                 | \$ (194,838)              | \$ 2,926,789                 | \$ 1,368,865  | \$ 4,755,655                            |

See Notes to Consolidated Condensed Financial Statements

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## PROTECTIVE LIFE CORPORATION

## CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

|   | For The Six Months Ended June 30, |                  |
|---|-----------------------------------|------------------|
|   | 2014                              | 2013             |
|   | (Dollars In Thousands)            |                  |
| <b>Cash flows from operating activities</b>   |                                   |                  |
| Net income  | \$ 191,616                        | \$ 181,490       |
| Adjustments to reconcile net income to net cash provided by operating activities:                   |                                   |                  |
| Realized investment losses (gains)  | 46,065                            | (28,559)         |
| Amortization of deferred policy acquisition costs and value of business acquired                    | 107,113                           | 127,185          |
| Capitalization of deferred policy acquisition costs   | (136,561)                         | (163,676)        |
| Depreciation expense  | 3,757                             | 4,404            |
| Deferred income tax   | (30,728)                          | 87,166           |
| Accrued income tax  | 91,410                            | 30,840           |
| Interest credited to universal life and investment products   | 422,306                           | 448,223          |
| Policy fees assessed on universal life and investment products                                      | (481,402)                         | (442,576)        |
| Change in reinsurance receivables   | 42,403                            | (26,793)         |
| Change in accrued investment income and other receivables   | (16,821)                          | 10,675           |
| Change in policy liabilities and other policyholders' funds of traditional life and health products | 83,825                            | 63,368           |
| Trading securities:   |                                   |                  |
| Maturities and principal reductions of investments  | 47,888                            | 101,838          |
| Sale of investments   | 112,473                           | 167,872          |
| Cost of investments acquired  | (75,742)                          | (245,520)        |
| Other net change in trading securities  | (52,325)                          | 13,544           |
| Change in other liabilities   | 104,961                           | (91,691)         |
| Other income - gains on repurchase of non-recourse funding obligations                              | (4,587)                           | (3,359)          |
| Other, net  | (32,161)                          | (43,064)         |
| <b>Net cash provided by operating activities</b>  | <b>423,490</b>                    | <b>191,367</b>   |
| <b>Cash flows from investing activities</b>   |                                   |                  |
| Maturities and principal reductions of investments, available-for-sale                              | 656,492                           | 489,364          |
| Sale of investments, available-for-sale   | 768,785                           | 1,336,778        |
| Cost of investments acquired, available-for-sale  | (2,071,692)                       | (2,684,864)      |
| Change in investments, held-to-maturity   | (35,000)                          | (35,000)         |
| Mortgage loans:   |                                   |                  |
| New lendings  | (351,505)                         | (171,997)        |
| Repayments  | 547,698                           | 345,704          |
| Change in investment real estate, net   | 1,256                             | 4,148            |
| Change in policy loans, net   | 37,365                            | 9,611            |
| Change in other long-term investments, net  | (73,387)                          | (122,295)        |
| Change in short-term investments, net   | (35,799)                          | 18,431           |
| Net unsettled security transactions   | 47,933                            | 51,883           |
| Purchase of property and equipment  | (4,776)                           | (10,865)         |
| Sales of property and equipment   | 57                                | 57               |
| Payments for business acquisitions  | (906)                             | -                |
| <b>Net cash used in investing activities</b>  | <b>(513,536)</b>                  | <b>(769,045)</b> |
| <b>Cash flows from financing activities</b>   |                                   |                  |
| Borrowings under line of credit arrangements and debt   | 90,000                            | 380,000          |
| Principal payments on line of credit arrangement and debt   | (230,000)                         | (320,000)        |
| Issuance (repayment) of non-recourse funding obligations  | 16,630                            | 18,900           |

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|   |                   |                   |
|---|-------------------|-------------------|
| Repurchase program borrowings                                     | 70,490            | 190,000           |
| Dividends to shareowners  | (34,649)          | (29,763)          |
| Investment product deposits and change in universal life deposits | 1,304,549         | 1,718,353         |
| Investment product withdrawals                                    | (1,232,428)       | (1,492,901)       |
| <b>Net cash (used in) provided by financing activities</b>        | <b>(15,408)</b>   | <b>464,589</b>    |
| <b>Change in cash</b>   | <b>(105,454)</b>  | <b>(113,089)</b>  |
| <b>Cash at beginning of period</b>                                | <b>466,542</b>    | <b>368,801</b>    |
| <b>Cash at end of period</b>                                      | <b>\$ 361,088</b> | <b>\$ 255,712</b> |

See Notes to Consolidated Condensed Financial Statements

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**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 six month periods ended June 30, 2014, are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. The year-end consolidated condensed financial 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, 2013.

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**

**Significant Accounting Policies**

For a full description of significant accounting policies, see Note 2 to consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013. There were no significant changes to the Company's accounting policies during the six months ended June 30, 2014.

**Accounting Pronouncements Not Yet Adopted**

**Accounting Standards Update ( ASU ) No. 2014-08 Reporting Discontinued Operations and Disclosure of Disposals of Components of an Entity.** This Update changes the requirements for reporting discontinued operations and related disclosures. The Update limits the definition of a discontinued operation to disposals that represent strategic shifts that will have a major effect on an entity's operation and financial results. Additionally, the Update requires enhanced disclosures about the components of discontinued operations and the financial effects of the disposal. The amendments in this Update are effective for annual and interim periods beginning after December 15, 2014. The Company is reviewing the additional disclosures required by the Update, and will apply the revised guidance to any disposals occurring after the effective date.

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**ASU No. 2014-09 Revenue from Contracts with Customers (Topic 606)**This Update provides for significant revisions to the recognition of revenue from contracts with customers across various industries. Under the new guidance, entities are required to apply a prescribed 5-step process to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The accounting for revenues associated with insurance products is not within the scope of this Update. The Update is effective for annual and interim periods beginning after December 15, 2016. The Company is reviewing its policies and processes to ensure compliance with the requirements in this Update.

**ASU No. 2014-11 Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures.** This Update changes the requirements for classification of certain repurchase agreements, and will expand the use of secured borrowing accounting for repurchase-to-maturity transactions. In addition, the Update requires additional disclosures for repurchase agreements accounted for both as sales and as secured borrowings. The amendments in this Update are effective for annual and interim periods beginning after December 15, 2014. The Update will not impact the Company's financial position or results of operations. The Company is reviewing its policies and processes to ensure compliance with the additional disclosure requirements in this Update.

**3. SIGNIFICANT ACQUISITIONS**

On October 1, 2013 Protective Life Insurance Company ( PLICO ) completed the acquisition contemplated by the master agreement (the Master Agreement ) dated April 10, 2013. Pursuant to that Master Agreement with AXA Financial, Inc. ( AXA ) and AXA Equitable Financial Services, LLC ( AEFS ), PLICO acquired the stock of MONY Life Insurance Company ( MONY ) from AEFS and entered into a reinsurance agreement (the Reinsurance Agreement ) pursuant to which it reinsured on a 100% indemnity reinsurance basis certain business (the MLOA Business ) of MONY Life Insurance Company of America ( MLOA ). The final aggregate purchase price of MONY was \$689 million. The ceding commission for the reinsurance of the MLOA Business was \$370 million. Together, the purchase of MONY and reinsurance of the MLOA Business are hereto referred to as (the MONY acquisition ). The MONY acquisition allowed the Company to invest its capital and increase the scale of its Acquisitions segment. The MONY acquisition business is comprised of traditional and universal life insurance policies and fixed and variable annuities, most of which were written prior to 2004.

The MONY acquisition was accounted for under the acquisition method of accounting under ASC Topic 805. In accordance with ASC 805-20-30, all identifiable assets acquired and liabilities assumed were measured at fair value as of the acquisition date. During the current quarter as a result of new information obtained about facts and circumstances that existed as of the acquisition date, the Company recorded certain measurement period adjustments to fixed maturities, mortgage loans, cash, accounts and premiums receivable, VOBA, other assets, deferred income taxes, future policy benefits and claims, other policyholders' funds, and other liabilities. These were customary adjustments that occurred during the normal course of reviewing and integrating the MONY acquisition. The net result on the amount of VOBA recorded by the Company in relation to the MONY acquisition was to decrease VOBA by approximately \$14.0 million. This impact has been revised in the comparative consolidated balance sheet presented as of December 31, 2013. The Company has determined that the impact on amortization and other related amounts within the comparative interim and annual periods from that previously presented in the annual or interim consolidated condensed statements of income is immaterial. The amounts presented in the following table related to the MONY acquisition (presented as of the acquisition date of October 1, 2013) have been retrospectively revised for the aforementioned measurement period adjustments.

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The following table summarizes the consideration paid for the acquisition and the determination of the fair value of assets acquired and liabilities assumed at the acquisition date:

|  | Fair Value<br>As of<br>October 1, 2013<br>(Dollars In Thousands) |                |
|--|--|----------------|
| <b>Assets</b>  |  |                |
| Fixed maturities, at fair value  | \$   | 6,557,853      |
| Equity securities, at fair value   |  | 108,413        |
| Mortgage loans   |  | 830,415        |
| Policy loans   |  | 967,534        |
| Short-term investments   |  | 130,963        |
| Total investments  |  | 8,595,178      |
| Cash   |  | 216,164        |
| Accrued investment income  |  | 114,695        |
| Accounts and premiums receivable, net of allowance for uncollectible amounts |  | 26,055         |
| Reinsurance receivables  |  | 422,692        |
| Value of business acquired   |  | 205,767        |
| Other assets   |  | 5,104          |
| Income tax receivables   |  | 21,197         |
| Deferred income taxes  |  | 188,142        |
| Separate account assets  |  | 195,452        |
| Total assets   | \$   | 9,990,446      |
| <b>Liabilities</b>   |  |                |
| Future policy benefits and claims  | \$   | 7,645,969      |
| Unearned premiums  |  | 3,066          |
| Total policy liabilities and accruals  |  | 7,649,035      |
| Annuity account balances   |  | 752,163        |
| Other policyholders' funds   |  | 636,448        |
| Other liabilities  |  | 66,124         |
| Non-recourse funding obligation  |  | 2,548          |
| Separate account liabilities   |  | 195,344        |
| Total liabilities  |  | 9,301,662      |
| <b>Net assets acquired</b>   | <b>\$</b>  | <b>688,784</b> |

The following (unaudited) pro forma condensed consolidated results of operations assumes that the aforementioned acquisition was completed as of January 1, 2012:

|               | Unaudited                                      |  |
|---------------|--|--|
|               | For The<br>Three Months Ended<br>June 30, 2013 | For The<br>Six Months Ended<br>June 30, 2013 |
|               | (Dollars In Thousands)                         |  |
| Revenue       | \$ 1,162,748                                   | \$ 2,316,066                                 |
| Net income    | \$ 120,589                                     | \$ 205,516                                   |
| EPS - basic   | \$ 1.52  | \$ 2.59                                      |
| EPS - diluted | \$ 1.49  | \$ 2.54                                      |





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**4. MONY CLOSED BLOCK OF BUSINESS**

In 1998, MONY converted from a mutual insurance company to a stock corporation ( demutualization ). In connection with its demutualization, an accounting mechanism known as a closed block (the Closed Block ) was established for certain individuals participating policies in force as of the date of demutualization. Assets, liabilities, and earnings of the Closed Block are specifically identified to support its participating policyholders. The Company acquired the Closed Block in conjunction with the MONY acquisition as discussed in Note 3, *Significant Acquisitions*.

Assets allocated to the Closed Block inure solely to the benefit of each Closed Block s policyholders and will not revert to the benefit of MONY or the Company. No reallocation, transfer, borrowing or lending of assets can be made between the Closed Block and other portions of MONY s general account, any of MONY s separate accounts or any affiliate of MONY without the approval of the Superintendent of The New York State Insurance Department (the Superintendent ). Closed Block assets and liabilities are carried on the same basis as similar assets and liabilities held in the general account.

The excess of Closed Block liabilities over Closed Block assets (adjusted to exclude the impact of related amounts in accumulated other comprehensive income (loss) ( AOCI )) at the acquisition date represented the estimated maximum future post-tax earnings from the Closed Block that would be recognized in income from continuing operations over the period the policies and contracts in the Closed Block remain in force. In connection with the acquisition of MONY, the Company has developed an actuarial calculation of the expected timing of MONY s Closed Block s earnings as of October 1, 2013.

If the actual cumulative earnings from the Closed Block are greater than the expected cumulative earnings, only the expected earnings will be recognized in the Company s net income. Actual cumulative earnings in excess of expected cumulative earnings at any point in time are recorded as a policyholder dividend obligation because they will ultimately be paid to Closed Block policyholders as an additional policyholder dividend unless offset by future performance that is less favorable than originally expected. If a policyholder dividend obligation has been previously established and the actual Closed Block earnings in a subsequent period are less than the expected earnings for that period, the policyholder dividend obligation would be reduced (but not below zero). If, over the period the policies and contracts in the Closed Block remain in force, the actual cumulative earnings of the Closed Block are less than the expected cumulative earnings, only actual earnings would be recognized in income from continuing operations. If the Closed Block has insufficient funds to make guaranteed policy benefit payments, such payments will be made from assets outside the Closed Block.

Many expenses related to Closed Block operations, including amortization of VOBA, are charged to operations outside of the Closed Block; accordingly, net revenues of the Closed Block do not represent the actual profitability of the Closed Block operations. Operating costs and expenses outside of the Closed Block are, therefore, disproportionate to the business outside of the Closed Block.

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Summarized financial information for the Closed Block from December 31, 2013 through June 30, 2014 is as follows:

|  | June 30, 2014          | As of | December 31, 2013 |
|--|------------------------|-------|-------------------|
|  | (Dollars In Thousands) |       |                   |
| <b>Closed block liabilities</b>  |                        |       |                   |
| Future policy benefits, policyholders' account balances and other  | \$ 6,195,402           |       | \$ 6,261,819      |
| Policyholder dividend obligation   | 328,872                |       | 190,494           |
| Other liabilities  | 59,751                 |       | 1,259             |
| Total closed block liabilities   | 6,584,025              |       | 6,453,572         |
| <b>Closed block assets</b>   |                        |       |                   |
| Fixed maturities, available-for-sale, at fair value  | \$ 4,402,851           |       | \$ 4,109,142      |
| Equity securities, available-for-sale, at fair value   | 5,369                  |       | 5,223             |
| Mortgage loans on real estate  | 512,800                |       | 601,959           |
| Policy loans   | 787,348                |       | 802,013           |
| Cash and other invested assets   | 70,954                 |       | 140,577           |
| Other assets   | 237,931                |       | 207,265           |
| Total closed block assets  | 6,017,253              |       | 5,866,179         |
| Excess of reported closed block liabilities over closed block assets   | 566,772                |       | 587,393           |
| Portion of above representing accumulated other comprehensive income:  |                        |       |                   |
| Net unrealized investment gains (losses) net of deferred tax benefit of \$0 and \$1,074 net of policyholder dividend obligation of \$86,196 and \$12,720 |                        |       | (1,994)           |
| Future earnings to be recognized from closed block assets and closed block liabilities   | \$ 566,772             |       | \$ 585,399        |

Reconciliation of the policyholder dividend obligation from December 31, 2013 through June 30, 2014 is as follows:

|  | For The<br>Six Months Ended<br>June 30, 2014<br>(Dollars In Thousands) |         |
|--|--|---------|
| Policyholder dividend obligation, at December 31, 2013   | \$   | 190,494 |
| Applicable to net revenue (losses)   |  | (6,951) |
| Change in net unrealized investment gains (losses) allocated to the policyholder dividend obligation |  | 145,329 |
| Policyholder dividend obligation, end of period  | \$   | 328,872 |

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Closed Block revenues and expenses were as follows:

|   | For The<br>Three Months Ended<br>June 30, 2014 | For The<br>Six Months Ended<br>June 30, 2014 |
|---|--|--|
|   | (Dollars In Thousands)                         |  |
| <b>Revenues</b>                         |  |  |
| Premiums and other income               | \$ 53,073                                      | \$ 102,846                                   |
| Net investment income                   | 60,416   | 112,623                                      |
| Net investment gains                    | 1,086  | 6,105  |
| Total revenues                          | 114,575  | 221,574                                      |
| <b>Benefits and other deduction</b>     |  |  |
| Benefits and settlement expenses        | 103,209  | 199,535                                      |
| Other operating expenses                | 383  | 90   |
| Total benefits and other deductions     | 103,592  | 199,625                                      |
| <b>Net revenues before income taxes</b> | <b>10,983</b>                                  | <b>21,949</b>                                |
| Income tax expense                      | 3,844  | 7,682  |
| <b>Net revenues</b>                     | <b>\$ 7,139</b>                                | <b>\$ 14,267</b>                             |

## 5. PROPOSED DAI-ICHI MERGER

On June 3, 2014, the Company entered into an Agreement and Plan of Merger (the "Merger Agreement") with The Dai-ichi Life Insurance Company, Limited, a *kabushiki kaisha* organized under the laws of Japan ("Dai-ichi") and DL Investment (Delaware), Inc., a Delaware corporation and wholly owned subsidiary of Dai-ichi which provides for the merger of DL Investment (Delaware), Inc. with and into the Company (the "Merger"), with the Company surviving the Merger as a wholly owned subsidiary of Dai-ichi.

The Company's Board of Directors unanimously (1) determined that the Merger and the other transactions contemplated by the Merger Agreement are fair to, advisable and in the best interests of, the Company and its shareowners, (2) approved the execution, delivery and performance of the Merger Agreement by the Company and the consummation of the Merger and the other transactions contemplated by the Merger Agreement, and (3) resolved to recommend the approval and adoption of the Merger Agreement and the transactions contemplated by the Merger Agreement by the shareowners of the Company. The Board of Directors received an opinion as to the fairness of the Merger consideration to be received by the shareowners of the Company from its financial advisor, Morgan Stanley & Co. LLC related to the terms of the Merger Agreement.

If the proposed Merger is completed, at the effective time of the Merger (the "Effective Time"), each share of the Company's common stock, par value \$0.50 per share, issued and outstanding immediately prior to the Effective Time, other than certain excluded shares, will be converted into the right to receive \$70 in cash, without interest (the "Per Share Merger Consideration"). Shares of common stock held by Dai-ichi or the Company or their respective direct or indirect wholly-owned subsidiaries will not be entitled to receive the Merger Consideration. Stock appreciation rights, restricted stock units and performance shares issued under various benefit plans will be paid out as described below under "Treatment of Benefit Plans".

Shareowners of the Company will be asked to vote on the adoption of the Merger Agreement and the Merger at a special shareowners meeting that will be held on a date to be announced. Completion of the Merger is subject to various closing conditions, including, but not limited to,

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(1) adoption of the Merger Agreement by the affirmative vote of the holders of at least a majority of all outstanding shares of the Company's common stock (the "Shareowner Approval"), (2) requisite approval of the Japan Financial Services Agency of an application and notification filing by Dai-ichi and its affiliates, (3) the receipt of certain insurance regulatory approvals, (4) the absence of any laws that have been adopted or promulgated, or any order, injunction, decision or decree issued or remaining in effect, that would prohibit the Merger or make the Merger illegal, and (5) the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, which waiting period terminated on July 25, 2014, pursuant to a grant of early termination by the Federal Trade Commission. Each party's obligation to consummate the Merger also is subject to certain additional conditions that include the accuracy of the other party's representations and warranties contained in the Merger Agreement (subject to certain materiality qualifiers) and the other party's compliance with its covenants and agreements contained in the Merger Agreement in all material respects. The Merger Agreement does not contain a financing condition.

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The Merger Agreement contains representations and warranties customary for transactions of this type. The Company has agreed to various customary covenants and agreements, including, among others, agreements to conduct its business in the ordinary course during the period between the execution of the Merger Agreement and the Effective Time, not to engage in certain kinds of transactions during this period, and to convene and hold a meeting of its shareowners for the purpose of obtaining the Shareowners Approval.

In addition, and subject to certain limitations, either party may terminate the Merger Agreement if the Merger is not consummated by February 28, 2015, which date is extended until April 30, 2015 in the event of delays in obtaining regulatory approval.

**Treatment of Benefit Plans**

Pursuant to the Merger Agreement, at or immediately prior to the Effective Time, each stock appreciation right with respect to shares of Common Stock granted under any Stock Plan (each, a SAR ) that is outstanding and unexercised immediately prior to the Effective Time and that has a base price per share of Common Stock underlying such SAR (the Base Price ) that is less than the Per Share Merger Consideration (each such SAR, an In-the-Money SAR ), whether or not exercisable or vested, will be cancelled and converted into the right to receive an amount in cash, without interest, determined by multiplying (i) the excess of the Per Share Merger Consideration over the Base Price of such In-the-Money SAR by (ii) the number of shares of Common Stock subject to such In-the-Money SAR (such amount, the SAR Consideration ). At the Effective Time, each SAR that has a Base Price that is equal to or greater than the Per Share Merger Consideration, whether or not exercisable or vested, will be cancelled and the holder of such SAR will not be entitled to receive any payment in exchange for such cancellation.

Pursuant to the Merger Agreement, at or immediately prior to the Effective Time, each restricted share unit with respect to a share of Common Stock granted under any Stock Plan (each, a RSU ) that is outstanding immediately prior to the Effective Time, whether or not vested, will be cancelled and converted into the right to receive an amount in cash, without interest, determined by multiplying (i) the Per Share Merger Consideration by (ii) the number of RSUs.

Pursuant to the Merger Agreement, at or immediately prior to the Effective Time, the number of performance shares earned for each award of performance shares granted under any Stock Plan will be calculated by determining the number of performance shares that would have been paid if the subject award period had ended on the December 31 immediately preceding the Effective Time (based on the conditions set for payment of performance share awards for the subject award period), provided that the number of performance shares earned for each award will not be less than the aggregate number of performance shares at the target performance level, and provided further that with respect to awards granted in the year in which the Effective Time occurs, performance shares will be earned at the same percentage as awards granted in the year preceding the year in which the Effective Time occurs. At or immediately prior to the Effective Time, each performance share so earned (each, a Performance Share ) that is outstanding immediately prior to the Effective Time, whether or not vested, will be cancelled and converted into the right to receive an amount in cash, without interest, determined by multiplying (i) the Per Share Merger Consideration by (ii) the number of Performance Shares.

Table of Contents**6. INVESTMENT OPERATIONS**

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

|   | For The<br>Three Months Ended<br>June 30, |              | For The<br>Six Months Ended<br>June 30, |              |
|---|---|--------------|---|--------------|
|   | 2014                                      | 2013         | 2014                                    | 2013         |
|   | (Dollars In Thousands)                    |              |   |              |
| Fixed maturities                            | \$ 20,198                                 | \$ 19,152    | \$ 27,568                               | \$ 31,461    |
| Equity securities                           |   | 2,366        |   | 2,367        |
| Impairments on fixed maturity securities    | (1,460)                                   | (2,910)      | (3,051)                                 | (6,497)      |
| Impairments on equity securities            |   | (1,090)      |   | (2,087)      |
| Modco trading portfolio                     | 60,989                                    | (126,694)    | 127,292                                 | (142,022)    |
| Other investments                           | (1,039)                                   | (4,802)      | (2,598)                                 | (5,929)      |
| Total realized gains (losses) - investments | \$ 78,688                                 | \$ (113,978) | \$ 149,211                              | \$ (122,707) |

For the three and six months ended June 30, 2014, gross realized gains on investments available-for-sale (fixed maturities, equity securities, and short-term investments) were \$20.4 million and \$28.1 million and gross realized losses were \$1.6 million and \$3.4 million, including \$1.4 million and \$2.9 million of impairment losses, respectively.

For the three and six months ended June 30, 2013, gross realized gains on investments available-for-sale (fixed maturities, equity securities, and short-term investments) were \$23.9 million and \$36.8 million and gross realized losses were \$6.2 million and \$11.1 million, including \$3.8 million and \$8.2 million of impairment losses, respectively.

For the three and six months ended June 30, 2014, the Company sold securities in an unrealized gain position with a fair value (proceeds) of \$306.3 million and \$571.0 million, respectively. The gain realized on the sale of these securities was \$20.4 million and \$28.1 million, respectively.

For the three and six months ended June 30, 2013, the Company sold securities in an unrealized gain position with a fair value (proceeds) of \$409.9 million and \$798.5 million, respectively. The gain realized on the sale of these securities was \$23.9 million and \$36.8 million, respectively.

For the three and six months ended June 30, 2014, the Company sold or otherwise disposed of securities in an unrealized loss position with a fair value (proceeds) of \$1.6 million and \$4.4 million, respectively. The losses realized on the sale of these securities were \$0.2 million and \$0.5 million, respectively. The Company made the decision to exit these holdings in conjunction with our overall asset liability management process.

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For the three and six months ended June 30, 2013, the Company sold securities in an unrealized loss position with a fair value (proceeds) of \$53.2 million and \$57.2 million, respectively. The losses realized on the sale of these securities were \$2.4 million and \$3.0 million, respectively. The Company made the decision to exit these holdings in conjunction with our overall asset liability management process.





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|                   | Amortized<br>Cost      | Unrealized<br>Gains | Unrealized<br>Losses | Fair<br>Value | Recognized<br>in OCI |
|-------------------|------------------------|---------------------|----------------------|---------------|----------------------|
|                   | (Dollars In Thousands) |                     |                      |               |                      |
| <b>2014</b>       |                        |                     |                      |               |                      |
| Fixed maturities: |                        |                     |                      |               |                      |
| Other             | \$ 400,000             | \$ 51,382           | \$                   | \$ 451,382    | \$                   |
|                   | \$ 400,000             | \$ 51,382           | \$                   | \$ 451,382    | \$                   |
| <b>2013</b>       |                        |                     |                      |               |                      |
| Fixed maturities: |                        |                     |                      |               |                      |
| Other             | \$ 365,000             | \$                  | \$ (29,324)          | \$ 335,676    | \$                   |
|                   | \$ 365,000             | \$                  | \$ (29,324)          | \$ 335,676    | \$                   |

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During the six months ended June 30, 2014 and the year ended December 31, 2013, the Company did not record any other-than-temporary impairments on held-to-maturity securities. The Company's held-to-maturity securities had no gross unrecognized holding losses for the period ended June 30, 2014 and \$29.3 million for the year ended December 31, 2013. The Company does not consider these unrecognized holding losses to be other-than-temporary based on certain positive factors associated with the securities which include credit ratings, financial health of the issuer, continued access of the issuer to capital markets and other pertinent information

As of June 30, 2014 and December 31, 2013, the Company had an additional \$2.9 billion and \$2.8 billion of fixed maturities, \$23.7 million and \$21.2 million of equity securities, and \$91.1 million and \$52.4 million of short-term investments classified as trading securities, respectively.

The amortized cost and fair value of available-for-sale and held-to-maturity fixed maturities as of June 30, 2014, 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.

|  | Available-for-sale     |               | Held-to-maturity       |            |
|--|------------------------|---------------|------------------------|------------|
|  | Amortized Cost         | Fair Value    | Amortized Cost         | Fair Value |
|  | (Dollars In Thousands) |               | (Dollars In Thousands) |            |
| Due in one year or less                | \$ 438,145             | \$ 448,757    | \$                     | \$         |
| Due after one year through five years  | 6,023,849              | 6,427,870     |                        |            |
| Due after five years through ten years | 8,650,531              | 9,173,945     |                        |            |
| Due after ten years                    | 16,276,874             | 18,259,166    | 400,000                | 451,382    |
|  | \$ 31,389,399          | \$ 34,309,738 | \$ 400,000             | \$ 451,382 |

During the three and six months ended June 30, 2014, the Company recorded pre-tax other-than-temporary impairments of investments of \$0.5 million and \$0.9 million, all of which related to fixed maturities, respectively. Credit impairments recorded in earnings during the three and six months ended June 30, 2014 were \$1.5 million and \$3.1 million, respectively. During the three and six months ended June 30, 2014, \$1.0 million and \$2.2 million of non-credit losses previously recorded in other comprehensive income (loss) were recorded in earnings as credit losses, respectively. For the three and six months ended June 30, 2014, there were no other-than-temporary impairments related to fixed maturities or equity securities that the Company intended to sell or expected to be required to sell.

During the three and six months ended June 30, 2013, the Company recorded pre-tax other-than-temporary impairments of investments of \$1.8 million and \$3.1 million, of which \$0.7 million and \$1.0 million related to debt securities and \$1.1 million and \$2.1 million related to equity securities, respectively. Credit impairments recorded in earnings during the three and six months ended June 30, 2013, were \$4.0 million and \$8.6 million, respectively. During the three and six months ended June 30, 2013, \$2.2 million and \$5.5 million of non-credit losses previously recorded in other comprehensive income were recorded in earnings as credit losses, respectively. For the three and six months ended June 30, 2013, there were no other-than-temporary impairments related to debt securities or equity securities that the Company intended to sell or expected to be required to sell.

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

|  | For The<br>Three Months Ended<br>June 30, |           | For The<br>Six Months Ended<br>June 30, |            |
|--|---|-----------|---|------------|
|  | 2014                                      | 2013      | 2014                                    | 2013       |
|  | (Dollars In Thousands)                    |           |   |            |
| Beginning balance  | \$ 20,839                                 | \$ 63,183 | \$ 41,692                               | \$ 122,121 |
| Additions for newly impaired securities  |   | 618       |   | 1,615      |
| Additions for previously impaired securities   | 553                                       | 1,568     | 1,027                                   | 3,054      |
| Reductions for previously impaired securities due to a change in expected cash flows | (3,407)                                   | (6,049)   | (24,734)                                | (67,470)   |
| Reductions for previously impaired securities that were sold in the current period   |   | (7,488)   |   | (7,488)    |
| Ending balance   | \$ 17,985                                 | \$ 51,832 | \$ 17,985                               | \$ 51,832  |

The following table includes the gross unrealized losses and fair value of the Company's investments that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of June 30, 2014:

|  | 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             | \$ 145,373             | \$ (10,089)     | \$ 94,770         | \$ (3,882)      | \$ 240,143   | \$ (13,971)     |
| Commercial mortgage-backed securities              | 37,107                 | (353)           | 126,051           | (3,670)         | 163,158      | (4,023)         |
| Other asset-backed securities                      | 121,233                | (6,982)         | 524,614           | (25,865)        | 645,847      | (32,847)        |
| U.S. government-related securities                 | 344,815                | (7,321)         | 314,356           | (14,464)        | 659,171      | (21,785)        |
| Other government-related securities                |                        |                 |                   |                 |              |                 |
| States, municipalities, and political subdivisions | 20,152                 | (1,641)         | 22,254            | (2,032)         | 42,406       | (3,673)         |
| Corporate bonds                                    | 815,310                | (24,098)        | 1,447,963         | (55,099)        | 2,263,273    | (79,197)        |
| Equities   | 105,413                | (3,741)         | 77,077            | (10,334)        | 182,490      | (14,075)        |
|  | \$ 1,589,403           | \$ (54,225)     | \$ 2,607,085      | \$ (115,346)    | \$ 4,196,488 | \$ (169,571)    |

RMBS have a gross unrealized loss greater than twelve months of \$3.9 million as of June 30, 2014. Factors such as the credit enhancement within the deal structure, the average life of the securities, and the performance of the underlying collateral support the recoverability of these investments.

CMBS have a gross unrealized loss greater than twelve months of \$3.7 million as of June 30, 2014. Factors such as the credit enhancement within the deal structure, the average life of the securities, and the performance of the underlying collateral support the recoverability of these investments.

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The other asset-backed securities have a gross unrealized loss greater than twelve months of \$25.9 million as of June 30, 2014. This category predominately includes student-loan backed auction rate securities, the underlying collateral, of which is at least 97% guaranteed by the Federal Family Education Loan Program ( FFELP ). These unrealized losses have occurred within the Company s auction rate securities ( ARS ) portfolio since the market collapse during 2008. At this time, the Company has no reason to believe that the U.S. Department of Education would not honor the FFELP guarantee, if it were necessary.

The U.S. government-related category has gross unrealized losses greater than twelve months of \$14.5 million as of June 30, 2014. These declines were entirely related to changes in interest rates.

The corporate bonds category has gross unrealized losses greater than twelve months of \$55.1 million as of June 30, 2014. These declines were primarily related to changes in interest rates during the period. The aggregate decline in market value of these securities was deemed temporary due to positive factors supporting the recoverability

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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.

The equities category has a gross unrealized loss greater than twelve months of \$10.3 million as of June 30, 2014. The aggregate decline in market value of these securities was deemed temporary due to factors supporting the recoverability of the respective investments. Positive factors include credit ratings, the financial health of the issuer, the continued access of the issuer to the capital markets, and other pertinent information.

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

The following table includes the gross unrealized losses and fair value of the Company's investments that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2013:

|  | Less Than 12 Months    |                    | 12 Months or More |                    | Total         |                    |
|--|------------------------|--------------------|-------------------|--------------------|---------------|--------------------|
|  | Fair<br>Value          | Unrealized<br>Loss | Fair<br>Value     | Unrealized<br>Loss | Fair<br>Value | Unrealized<br>Loss |
|  | (Dollars In Thousands) |                    |                   |                    |               |                    |
| Residential mortgage-backed securities             | \$ 333,235             | \$ (14,051)        | \$ 210,486        | \$ (10,513)        | \$ 543,721    | \$ (24,564)        |
| Commercial mortgage-backed securities              | 429,228                | (18,467)           | 13,840            | (1,238)            | 443,068       | (19,705)           |
| Other asset-backed securities                      | 175,846                | (14,555)           | 497,512           | (54,993)           | 673,358       | (69,548)           |
| U.S. government-related securities                 | 891,698                | (53,508)           | 6,038             | (570)              | 897,736       | (54,078)           |
| Other government-related securities                | 10,161                 | (1)                |                   |                    | 10,161        | (1)                |
| States, municipalities, and political subdivisions | 172,157                | (8,113)            | 335               | (178)              | 172,492       | (8,291)            |
| Corporate bonds                                    | 7,484,010              | (353,211)          | 272,423           | (38,856)           | 7,756,433     | (392,067)          |
| Equities   | 376,776                | (27,861)           | 21,974            | (8,501)            | 398,750       | (36,362)           |
|  | \$ 9,873,111           | \$ (489,767)       | \$ 1,022,608      | \$ (114,849)       | \$ 10,895,719 | \$ (604,616)       |

RMBS had a gross unrealized loss greater than twelve months of \$10.5 million as of December 31, 2013. Factors such as the credit enhancement within the deal structure, the average life of the securities, and the performance of the underlying collateral support the recoverability of these investments.

CMBS had a gross unrealized loss greater than twelve months of \$1.2 million as of December 31, 2013. Factors such as the credit enhancement within the deal structure, the average life of the securities, and the performance of the underlying collateral support the recoverability of these investments.

The other asset-backed securities had a gross unrealized loss greater than twelve months of \$55.0 million as of December 31, 2013. This category predominately includes student-loan backed auction rate securities, the underlying collateral, of which is at least 97% guaranteed by the FFELP. These unrealized losses have occurred within the Company's ARS portfolio since the market collapse during 2008. At this time, the Company has no reason to believe that the U.S. Department of Education would not honor the FFELP guarantee, if it were necessary.

The corporate bonds category had gross unrealized losses greater than twelve months of \$38.9 million as of December 31, 2013. 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.

The equities category had a gross unrealized loss greater than twelve months of \$8.5 million as of December 31, 2013. The aggregate decline in market value of these securities was deemed temporary due to factors supporting the recoverability of the respective investments. Positive factors include credit ratings, the financial health of the issuer, the continued access of the issuer to the capital markets, and other pertinent information.

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

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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 June 30, 2014, the Company had securities in its available-for-sale portfolio which were rated below investment grade of \$1.7 billion and had an amortized cost of \$1.7 billion. In addition, included in the Company's trading portfolio, the Company held \$334.5 million of securities which were rated below investment grade. Approximately \$817.9 million of the below investment grade securities were not publicly traded.

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

|                   | For The<br>Three Months Ended<br>June 30, |              | For The<br>Six Months Ended<br>June 30, |                |
|-------------------|---|--------------|---|----------------|
|                   | 2014                                      | 2013         | 2014                                    | 2013           |
|                   | (Dollars In Thousands)                    |              |   |                |
| Fixed maturities  | \$ 519,745                                | \$ (849,033) | \$ 1,148,357                            | \$ (1,018,822) |
| Equity securities | 14,591                                    | (8,392)      | 33,004                                  | (4,602)        |

**Variable Interest Entities**

The Company holds certain investments in entities in which its ownership interests could possibly be considered variable interests under Topic 810 of the Financial Accounting Standards Board ( FASB ) Accounting Standard Codification ( ASC or Codification ) (excluding debt and equity securities held as trading, available for sale, or held to maturity). The Company reviews the characteristics of each of these applicable entities and compares those characteristics to applicable criteria to determine whether the entity is a Variable Interest Entity ( VIE ). If the entity is determined to be a VIE, the Company then performs a detailed review 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 is the primary beneficiary. ASC 810 provides that an entity is the primary beneficiary of a VIE if the entity has 1) 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 an interest in one wholly owned subsidiary, Red Mountain, LLC ( Red Mountain ), that was classified as a VIE as of June 30, 2014 and December 31, 2013. The activity most significant to Red Mountain is the issuance of a note in connection with a financing transaction involving Golden Gate V Vermont Captive Insurance Company ( Golden Gate V ) and the Company in which Golden Gate V issued non-recourse funding obligations to Red Mountain and Red Mountain issued the note to Golden Gate V. Credit enhancement on the Red Mountain Note is provided by an unrelated third party. For details of this transaction, see Note 9, *Debt and Other Obligations*. The Company had the power, via its 100% ownership through an affiliate, to direct the activities of the VIE, but did not have the obligation to absorb losses related to the primary risks or sources of variability to the VIE. The variability of loss would be borne primarily by the third party in its function as provider of credit enhancement on the Red Mountain Note. Accordingly, it was determined that the Company is not the primary beneficiary of the VIE. The Company's risk of loss related to the VIE is limited to its investment of \$10,000. Additionally, the holding company ( PLC ) has guaranteed the VIE's payment obligation for the credit enhancement fee to the unrelated third party provider. As of June 30, 2014, no payments have been made or required related to this guarantee.



**7. MORTGAGE LOANS**

**Mortgage Loans**

The Company invests a portion of its investment portfolio in commercial mortgage loans. As of June 30, 2014, the Company's mortgage loan holdings were approximately \$5.3 billion. The Company has specialized in making loans

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on either credit-oriented commercial properties or credit-anchored strip shopping centers and apartments. The Company's underwriting procedures relative to its commercial loan portfolio are based, in the Company's view, on a conservative and disciplined approach. The Company concentrates on a small number of commercial real estate asset types associated with the necessities of life (retail, multi-family, professional office buildings, and warehouses). The Company believes these asset types tend to weather economic downturns better than other commercial asset classes in which it has chosen not to participate. The Company believes this disciplined approach has helped to maintain a relatively low delinquency and foreclosure rate throughout its history. The majority of the Company's mortgage loans portfolio was underwritten and funded by the Company. From time to time, the Company may acquire loans in conjunction with an acquisition.

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

Certain of our mortgage loans have call options or interest rate reset options between 3 and 10 years. However, if interest rates were to significantly increase, we may be unable to exercise the call options or increase the interest rates on our existing mortgage loans commensurate with the significantly increased market rates. Assuming the loans are called at their next call dates, approximately \$43.7 million would become due for the remainder of 2014, \$1.1 billion in 2015 through 2019, \$501.4 million in 2020 through 2024, and \$130.5 million thereafter.

The Company offers a type of commercial mortgage loan under which the Company will permit a loan-to-value ratio of up to 85% in exchange for a participating interest in the cash flows from the underlying real estate. As of June 30, 2014 and December 31, 2013, approximately \$613.8 million and \$666.6 million, respectively, of the Company's mortgage loans have this participation feature. Cash flows received as a result of this participation feature are recorded as interest income. During the three and six months ended June 30, 2014 and 2013, the Company recognized \$2.8 million, \$5.8 million, \$5.8 million, and \$9.2 million, respectively, of participating mortgage loan income.

As of June 30, 2014, approximately \$5.9 million, or 0.01%, of invested assets consisted of nonperforming, restructured or mortgage loans that were foreclosed and were converted to real estate properties. The Company does not expect these investments to adversely affect its liquidity or ability to maintain proper matching of assets and liabilities. During the six months ended June 30, 2014, certain mortgage loan transactions occurred that were accounted for as troubled debt restructurings under Topic 310 of the FASB ASC. For all mortgage loans, the impact of troubled debt restructurings is generally reflected in our investment balance and in the allowance for mortgage loan credit losses. Transactions accounted for as troubled debt restructurings during the quarter included acceptance of assets in satisfaction of principal, and were the result of agreements between the creditor and the debtor. During the three and six month periods ending June 30, 2014, the Company accepted assets of \$15.1 million in satisfaction of \$16.0 million of principal resulting in a \$0.9 million decrease in the Company's investment in mortgage loans net of existing allowances for mortgage loan losses. No loans classified as troubled debt restructurings remained on the Company's balance sheet as of June 30, 2014.

The Company's mortgage loan portfolio consists of two categories of loans: (1) those not subject to a pooling and servicing agreement and (2) those subject to a contractual pooling and servicing agreement. As of June 30, 2014, \$3.7 million of mortgage loans not subject to a pooling and servicing agreement were nonperforming or restructured. None of these nonperforming loans have been restructured during the six months ended June 30, 2014. The Company did not foreclose on any loans during the six months ended June 30, 2014.

As of June 30, 2014, \$2.2 million of loans subject to a pooling and servicing agreement were nonperforming. None of these nonperforming loans have been restructured during the six months ended June 30, 2014. The Company did not foreclose on any loans during the six months ended

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June 30, 2014.

As of June 30, 2014 and December 31, 2013, the Company had an allowance for mortgage loan credit losses of \$4.3 million and \$3.1 million, respectively. Due to the Company's loss experience and nature of the loan portfolio, the Company believes that a collectively evaluated allowance would be inappropriate. The Company believes an

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

A charge off is recorded by eliminating the allowance against the mortgage loan and recording the renegotiated loan or the collateral property related to the loan as investment real estate on the balance sheet, which is carried at the lower of the appraised fair value of the property or the unpaid principal balance of the loan, less estimated selling costs associated with the property:

|                   | As of                  |                   |
|-------------------|------------------------|-------------------|
|                   | June 30, 2014          | December 31, 2013 |
|                   | (Dollars In Thousands) |                   |
| Beginning balance | \$ 3,130               | \$ 2,875          |
| Charge offs       |                        | (6,838)           |
| Recoveries        | (1,075)                | (1,016)           |
| Provision         | 2,225                  | 8,109             |
| Ending balance    | \$ 4,280               | \$ 3,130          |

It is the Company's policy to cease to carry accrued interest on loans that are over 90 days delinquent. For loans less than 90 days delinquent, interest is accrued unless it is determined that the accrued interest is not collectible. If a loan becomes over 90 days delinquent, it is the Company's general policy to initiate foreclosure proceedings unless a workout arrangement to bring the loan current is in place. For loans subject to a pooling and servicing agreement, there are certain additional restrictions and/or requirements related to workout proceedings, and as such, these loans may have different attributes and/or circumstances affecting the status of delinquency or categorization of those in nonperforming status. An analysis of the delinquent loans is shown in the following chart as of June 30, 2014.

|  | 30-59 Days<br>Delinquent | 60-89 Days<br>Delinquent | Greater<br>than 90 Days<br>Delinquent | Total<br>Delinquent |
|--|--------------------------|--------------------------|---------------------------------------|---------------------|
|  | (Dollars In Thousands)   |                          |                                       |                     |
| Commercial mortgage loans                      | \$ 24,562                | \$                       | \$ 5,908                              | \$ 30,470           |
| Number of delinquent commercial mortgage loans | 9                        |                          | 4                                     | 13                  |

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The Company's commercial mortgage loan portfolio consists of mortgage loans that are collateralized by real estate. Due to the collateralized nature of the loans, any assessment of impairment and ultimate loss given a default on the loans is based upon a consideration of the estimated fair value of the real estate. The Company limits accrued interest income on impaired loans to 90 days of interest. Once accrued interest on the impaired loan is received, interest income is recognized on a cash basis. For information regarding impaired loans, please refer to the following chart as of June 30, 2014 and December 31, 2013:

|                                    | Recorded<br>Investment | Unpaid<br>Principal<br>Balance | Related<br>Allowance<br>(Dollars In Thousands) | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized | Cash Basis<br>Interest<br>Income |
|------------------------------------|------------------------|--------------------------------|--|-----------------------------------|----------------------------------|----------------------------------|
| <b>2014</b>                        |                        |                                |  |                                   |                                  |                                  |
| Commercial mortgage loans:         |                        |                                |  |                                   |                                  |                                  |
| With no related allowance recorded | \$ 5,275               | \$ 5,254                       | \$   | \$ 1,758                          | \$ 64                            | \$ 43                            |
| With an allowance recorded         | 23,754                 | 23,738                         | 4,280  | 3,959                             | 314                              | 314                              |
| <b>2013</b>                        |                        |                                |  |                                   |                                  |                                  |
| Commercial mortgage loans:         |                        |                                |  |                                   |                                  |                                  |
| With no related allowance recorded | \$ 2,208               | \$ 2,208                       | \$   | \$ 2,208                          | \$ 31                            | \$                               |
| With an allowance recorded         | 21,288                 | 21,281                         | 3,130  | 5,322                             | 304                              | 304                              |

**8. GOODWILL**

During the six months ended June 30, 2014, the Company decreased its goodwill balance by approximately \$1.5 million. The decrease was due to an adjustment in the Acquisitions segment related to tax benefits realized during 2014 on the portion of tax goodwill in excess of GAAP basis goodwill. As of June 30, 2014, the Company had an aggregate goodwill balance of \$103.9 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 first determines through qualitative analysis whether relevant events and circumstances indicate that it is more likely than not that segment goodwill balances are impaired as of the testing date. If it is determined that it is more likely than not that impairment exists, the Company compares its estimate of the fair value of the reporting unit to which the goodwill is assigned to the reporting unit's carrying amount, including goodwill. The Company utilizes a fair value measurement (which includes a discounted cash flows analysis) to assess the carrying value of the reporting units in consideration of the recoverability of the goodwill balance assigned to each reporting unit as of the measurement date. The Company's material goodwill balances are attributable to certain of its operating segments (which are each considered to be reporting units). The cash flows used to determine the fair value of the Company's reporting units are dependent on a number of significant assumptions. The Company's estimates, which consider a market participant view of fair value, are subject to change given the inherent uncertainty in predicting future results and cash flows, which are impacted by such things as policyholder behavior, competitor pricing, capital limitations, new product introductions, and specific industry and market conditions. Additionally, the discount rate used is based on the Company's judgment of the appropriate rate for each reporting unit based on the relative risk associated with the projected cash flows. As of December 31, 2013, the Company performed its annual evaluation of goodwill and determined that no adjustment to impair goodwill was necessary. During the six months ended June 30, 2014, no events occurred which indicate an impairment was required or which would invalidate the previous results of the Company's impairment assessment.

**9. DEBT AND OTHER OBLIGATIONS**

The Company has access to a Credit Facility that provides the ability to borrow on an unsecured basis up to an aggregate principal amount of \$750 million. The Company has the right in certain circumstances to request that the

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commitment under the Credit Facility be increased up to a maximum principal amount of \$1.0 billion. Balances outstanding under the Credit Facility accrue interest at a rate equal to, at the option of the Borrowers, (i) LIBOR plus a spread based on the ratings of the Company's senior unsecured long-term debt (Senior Debt), or (ii) the sum of (A) a rate equal to the highest of (x) the Administrative Agent's prime rate, (y) 0.50% above the Federal Funds rate, or (z) the one-month LIBOR plus 1.00% and (B) a spread based on the ratings of the Company's Senior Debt. The Credit Facility also provides for a facility fee at a rate that varies with the ratings of the Company's Senior Debt and that is calculated on the aggregate amount of commitments under the Credit Facility, whether used or unused. The maturity date on the Credit Facility is July 17, 2017. The Company is not aware of any non-compliance with the financial debt covenants of the Credit Facility as of June 30, 2014. There was an outstanding balance of \$345.0 million at an interest rate of LIBOR plus 1.20% under the Credit Facility as of June 30, 2014.

**Non-Recourse Funding Obligations**

*Golden Gate II Captive Insurance Company*

Golden Gate II Captive Insurance Company (Golden Gate II), a special purpose financial captive insurance company wholly owned by PLICO, had \$575 million of outstanding non-recourse funding obligations as of June 30, 2014. These outstanding non-recourse funding obligations were issued to special purpose trusts, which in turn issued securities to third parties. Certain of our affiliates own a portion of these securities. As of June 30, 2014, securities related to \$176.6 million of the outstanding balance of the non-recourse funding obligations were held by external parties and securities related to \$398.4 million of the non-recourse funding obligations were held by our affiliates. The Company has entered into certain support agreements with Golden Gate II obligating the Company to make capital contributions or provide support related to certain of Golden Gate II's expenses and in certain circumstances, to collateralize certain of the Company's obligations to Golden Gate II. These support agreements provide that amounts would become payable by the Company to Golden Gate II if its annual general corporate expenses were higher than modeled amounts or if Golden Gate II's investment income on certain investments or premium income was below certain actuarially determined amounts. As of June 30, 2014, no payments have been made under these agreements.

*Golden Gate V Vermont Captive Insurance Company*

On October 10, 2012, Golden Gate V and Red Mountain, indirect wholly owned subsidiaries of the Company, entered into a 20-year transaction to finance up to \$945 million of AXXX reserves related to a block of universal life insurance policies with secondary guarantees issued by our direct wholly owned subsidiary PLICO and indirect wholly owned subsidiary, West Coast Life Insurance Company (WCL). Golden Gate V issued non-recourse funding obligations to Red Mountain, and Red Mountain issued a note with an initial principal amount of \$275 million, increasing to a maximum of \$945 million in 2027, to Golden Gate V for deposit to a reinsurance trust supporting Golden Gate V's obligations under a reinsurance agreement with WCL, pursuant to which WCL cedes liabilities relating to the policies of WCL and retrocedes liabilities relating to the policies of PLICO. Through the structure, Hannover Life Reassurance Company of America (Hannover Re), the ultimate risk taker in the transaction, provides credit enhancement to the Red Mountain note for the 20-year term in exchange for a fee. The transaction is non-recourse to Golden Gate V, Red Mountain, WCL, PLICO and the Company, meaning that none of these companies are liable for the reimbursement of any credit enhancement payments required to be made. As of June 30, 2014, the principal balance of the Red Mountain note was \$400 million. In connection with the transaction, the Company has entered into certain support agreements under which it guarantees or otherwise supports certain obligations of Golden Gate V or Red Mountain. Future scheduled capital contributions to prefund credit enhancement fees amount to approximately \$144.3 million and will be paid in annual installments through 2031. The support agreements provide that amounts would become payable by the Company if Golden Gate V's annual general corporate expenses were higher than modeled amounts or in the event write-downs due to other-than-temporary impairments on assets held in certain accounts exceed defined threshold levels. Additionally, the Company has entered into separate agreements to indemnify Golden Gate V with respect to material adverse changes in non-guaranteed elements of insurance policies reinsured by Golden Gate V, and to guarantee payment of certain fee amounts in connection with the credit enhancement of the Red Mountain note. As of June 30, 2014, no payments have been made under these agreements.

In connection with the transaction outlined above, Golden Gate V had a \$400 million outstanding non-recourse funding obligation as of June 30, 2014. This non-recourse funding obligation matures in 2037, has scheduled increases in principal to a maximum of \$945 million, and accrues interest at a fixed annual rate of 6.25%.



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Non-recourse funding obligations outstanding as of June 30, 2014, on a consolidated basis, are shown in the following table:

| Issuer   | Balance<br>(Dollars In Thousands) | Maturity<br>Year | Year-to-Date<br>Weighted-Avg<br>Interest Rate |
|--|-----------------------------------|------------------|---|
| Golden Gate II Captive Insurance Company           | \$ 176,552                        | 2052             | 1.12%   |
| Golden Gate V Vermont Captive Insurance Company(1) | 400,000                           | 2037             | 6.25%   |
| MONY Life Insurance Company(1)                     | 2,526                             | 2024             | 6.63%   |
| Total  | \$ 579,078                        |                  |   |

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(1) Fixed rate obligations

During the six months ended June 30, 2014, the Company repurchased \$18.3 million of its outstanding non-recourse funding obligations, at a discount, all of which was purchased in the current quarter. The repurchased resulted in a \$4.6 million pre-tax gain for the Company. For the six months ended June 30, 2013, the Company repurchased \$16.1 million of its outstanding non-recourse funding obligations, at a discount. The repurchase resulted in a \$3.4 million pre-tax gain for the Company. These gains are recorded in other income in the consolidated condensed statements of income.

### Letters of Credit

Golden Gate III Vermont Captive Insurance Company ( Golden Gate III ), a Vermont special purpose financial insurance company and wholly owned subsidiary of PLICO, is party to a Reimbursement Agreement (the Reimbursement Agreement ) with UBS AG, Stamford Branch ( UBS ), as issuing lender. Under the original Reimbursement Agreement, dated April 23, 2010, UBS issued a letter of credit (the LOC ) in the initial amount of \$505 million to a trust for the benefit of WCL. The Reimbursement Agreement was subsequently amended and restated effective November 21, 2011 (the First Amended and Restated Reimbursement Agreement ), to replace the existing LOC with one or more letters of credit from UBS, and to extend the maturity date from April 1, 2018, to April 1, 2022. On August 7, 2013, the Company entered into a Second Amended and Restated Reimbursement Agreement with UBS (the Second Amended and Restated Reimbursement Agreement ), which amended and restated the First Amended and Restated Reimbursement Agreement. Under the Second and Amended and Restated Reimbursement Agreement a new LOC in an initial amount of \$710 million was issued by UBS in replacement of the existing LOC issued under the First Amended and Restated Reimbursement Agreement. The term of the LOC was extended from April 1, 2022 to October 1, 2023, subject to certain conditions being satisfied including scheduled capital contributions being made to Golden Gate III by one of its affiliates. The maximum stated amount of the LOC was increased from \$610 million to \$720 million in 2015 if certain conditions are met. On June 25, 2014, the Company entered into a Third Amended and Restated Reimbursement Agreement with UBS (the Third Amended and Restated Reimbursement Agreement ), which amended and restated the Second Amended and Restated Reimbursement Agreement. Under the Third Amended and Restated Reimbursement Agreement, a new LOC in an initial amount of \$915 million was issued by UBS in replacement of the existing LOC issued under the Second Amended and Restated Reimbursement Agreement. The term of the LOC was extended from October 1, 2023 to April 1, 2025, subject to certain conditions being satisfied including scheduled capital contributions being made to Golden Gate III by one of its affiliates. The maximum stated amount of the LOC was increased from \$720 million to \$935 million in 2015 if certain conditions are met. The LOC is held in trust for the benefit of WCL, and supports certain obligations of Golden Gate III to WCL under an indemnity reinsurance agreement originally effective April 1, 2010, as amended and restated on November 21, 2011, and as further amended and restated on August 7, 2013 and on June 25, 2014 to include additional blocks of policies, and pursuant to which WCL cedes liabilities relating to the policies of WCL and retrocedes liabilities relating to the policies of PLICO. The LOC balance was \$915 million as of June 30, 2014. Subject to certain conditions, the amount of the LOC will be periodically increased up to a maximum of \$935 million in 2015. The term of the LOC is expected to be approximately 15 years from the original issuance date. This transaction is non-recourse to WCL, PLICO, and the Company, meaning that

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none of these companies other than Golden Gate III are liable for reimbursement on a draw of the LOC. The Company has entered into certain support agreements with Golden Gate III obligating the Company to make capital contributions or provide support related to certain of Golden Gate III's expenses and in certain circumstances, to collateralize certain of the Company's obligations to Golden Gate III. Future scheduled capital

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contributions amount to approximately \$122.5 million and will be paid in three installments with the last payment occurring in 2021, and these contributions may be subject to potential offset against dividend payments as permitted under the terms of the Third Amended and Restated Reimbursement Agreement. The support agreements provide that amounts would become payable by the Company to Golden Gate III if its annual general corporate expenses were higher than modeled amounts or if specified catastrophic losses occur during defined time periods with respect to the policies reinsured by Golden Gate III. Pursuant to the terms of an amended and restated letter agreement with UBS, the Company has continued to guarantee the payment of fees to UBS as specified in the Third Amended and Restated Reimbursement Agreement. As of June 30, 2014, no payments have been made under these agreements.

Golden Gate IV Vermont Captive Insurance Company ( Golden Gate IV ), a Vermont special purpose financial insurance company and wholly owned subsidiary of PLICO, is party to a Reimbursement Agreement with UBS AG, Stamford Branch, as issuing lender. Under the Reimbursement Agreement, dated December 10, 2010, UBS issued an LOC in the initial amount of \$270 million to a trust for the benefit of WCL. The LOC balance increased, in accordance with the terms of the Reimbursement Agreement, during the second quarter of 2014 and was \$730 million as of June 30, 2014. Subject to certain conditions, the amount of the LOC will be periodically increased up to a maximum of \$790 million in 2016. The term of the LOC is expected to be 12 years from the original issuance date (stated maturity of December 30, 2022). The LOC was issued to support certain obligations of Golden Gate IV to WCL under an indemnity reinsurance agreement, pursuant to which WCL cedes liabilities relating to the policies of WCL and retrocedes liabilities relating to the policies of PLICO. This transaction is non-recourse to WCL, PLICO, and the Company, meaning that none of these companies other than Golden Gate IV are liable for reimbursement on a draw of the LOC. The Company has entered into certain support agreements with Golden Gate IV obligating the Company to make capital contributions or provide support related to certain of Golden Gate IV's expenses and in certain circumstances, to collateralize certain of the Company's obligations to Golden Gate IV. The support agreements provide that amounts would become payable by the Company to Golden Gate IV if its annual general corporate expenses were higher than modeled amounts or if specified catastrophic losses occur during defined time periods with respect to the policies reinsured by Golden Gate IV. The Company has also entered into a separate agreement to guarantee the payments of LOC fees under the terms of the Reimbursement Agreement. As of June 30, 2014, no payments have been made under these agreements.

**Repurchase Program Borrowings**

While the Company anticipates that the cash flows of its operating subsidiaries will be sufficient to meet its investment commitments and operating cash needs in a normal credit market environment, the Company recognizes that investment commitments scheduled to be funded may, from time to time, exceed the funds then available. Therefore, the Company has established repurchase agreement programs for certain of its insurance subsidiaries to provide liquidity when needed. The Company expects that the rate received on its investments will equal or exceed its borrowing rate. Under this program, the Company may, from time to time, sell an investment security at a specific price and agree to repurchase that security at another specified price at a later date. These borrowings are for a term less than ninety days. The market value of securities to be repurchased is monitored and collateral levels are adjusted where appropriate to protect the counterparty against credit exposure. Cash received is invested in fixed maturity securities, and the agreements provided for net settlement in the event of default or on termination of the agreements. As of June 30, 2014, the fair value of securities pledged under the repurchase program was \$476.3 million and the repurchase obligation of \$420.5 million was included in the Company's consolidated condensed balance sheets (at an average borrowing rate of 11 basis points). During the six months ended June 30, 2014, the maximum balance outstanding at any one point in time related to these programs was \$633.7 million. The average daily balance was \$510.2 million (at an average borrowing rate of 10 basis points) during the six months ended June 30, 2014. As of December 31, 2013, the Company had a \$350.0 million outstanding balance related to such borrowings. During 2013, the maximum balance outstanding at any one point in time related to these programs was \$815.0 million. The average daily balance was \$496.9 million (at an average borrowing rate of 11 basis points) during the year ended December 31, 2013.

**10. COMMITMENTS AND CONTINGENCIES**

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The Company has entered into indemnity agreements with each of its current directors that provide, among other things and subject to certain limitations, a contractual right to indemnification to the fullest extent permissible under the law. The Company has agreements with certain of its officers providing up to \$10 million in indemnification.

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These obligations are in addition to the customary obligation to indemnify officers and directors contained in the Company's governance documents.

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

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

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

Since the entry into the Merger Agreement on June 3, 2014, four lawsuits have been filed against the Company, our directors, Dai-ichi and DL Investment (Delaware), Inc. on behalf of alleged Company shareowners. On June 11, 2014, a putative class action lawsuit styled *Edelman, et al. v. Protective Life Corporation, et al.*, Civil Action No. 01-CV-2014-902474.00, was filed in the Circuit Court of Jefferson County, Alabama. On July 30, 2014, the plaintiff in *Edelman* filed an amended complaint. Three putative class action lawsuits have been filed in the Court of Chancery of the State of Delaware, including *Martin, et al. v. Protective Life Corporation, et al.*, Civil Action No. 9794-CB, filed June 19, 2014, *Leyendecker, et al. v. Protective Life Corporation, et al.*, Civil Action No. 9931-CB, filed July 22, 2014 and *Hilburn, et al. v. Protective Life Corporation, et al.*, Civil Action No. 9937-CB, filed July 23, 2014. The Delaware Court of Chancery consolidated the *Martin*, *Leyendecker* and *Hilburn* actions under the caption *In re Protective Life Corp. Stockholders Litigation*, Consolidated Civil Action No. 9794-CB, designated the *Hilburn* complaint as the operative consolidated complaint and appointed Charlotte Martin, Samuel J. Leyendecker, Jr., and Deborah J. Hilburn to serve as co-lead plaintiffs. These lawsuits allege that our Board of Directors breached its fiduciary duties to our shareowners, that the Merger involves an unfair price, an inadequate sales process, and unreasonable deal protection devices that purportedly preclude competing offers, and that the preliminary proxy statement filed with the SEC on July 10, 2014 fails to disclose purportedly material information. The complaints also allege that the Company, Dai-ichi and DL Investment (Delaware), Inc. aided and abetted those alleged breaches of fiduciary duties. The complaints seek injunctive relief, including enjoining or rescinding the Merger, and attorneys' and other fees and costs, in addition to other relief. The consolidated Delaware action also seeks an award of unspecified damages. The Company and our Board of Directors believe these claims are without merit and intend to vigorously defend these actions. The Company cannot predict the outcome of or estimate the possible loss or range of loss from these matters.

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

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The Company was audited by the IRS and the IRS proposed favorable and unfavorable adjustments to the Company's 2003 through 2007 reported taxable income. The Company protested certain unfavorable adjustments and sought resolution at the IRS Appeals Division. The case has followed normal procedure and is now under review at Congress Joint Committee on Taxation. The Company believes the matter will conclude within the next twelve months. If the IRS prevails on every issue that it identified in this audit, and the Company does not litigate these issues, then the Company will make an income tax payment of approximately \$26.6 million. However, this payment, if it were to occur, would not materially impact the Company or its effective tax rate.

Through the acquisition of MONY by PLICO certain income tax credit carryforwards, which arose in MONY's pre-acquisition tax years, transferred to the Company. This transfer was in accordance with the applicable rules of the Internal Revenue Code and the related Regulations. In spite of this transfer, AXA, the former parent of the consolidated income tax return group in which MONY was a member, retains the right to utilize these credits in the future to offset future increases in its 2010 through 2013 tax liabilities. The Company had determined that, based on all information known as of the acquisition date and through the March 31, 2014 reporting date, it was probable that a loss of the utilization of these carryforwards had been incurred. Due to indemnification received from AXA during the quarter ending June 30, 2014, the probability of loss of these carryforwards has been eliminated. Accordingly, in the table summarizing the fair value of net assets acquired from the Acquisition, the amount of the deferred tax asset from the credit carryforwards is no longer offset by a liability.

The Company has received notice from two third party auditors that certain of the Company's insurance subsidiaries, as well as certain other insurance companies for which the Company has co-insured blocks of life insurance and annuity policies, are under audit for compliance with the unclaimed property laws of a number of states. The audits are being conducted on behalf of the treasury departments or unclaimed property administrators in such states. The focus of the audits is on whether there have been unreported deaths, maturities, or policies that have exceeded limiting age with respect to which death benefits or other payments under life insurance or annuity policies should be treated as unclaimed property that should be escheated to the state. The Company has recorded a reserve with respect to life insurance policies issued by the Company's subsidiaries and certain co-insured blocks of life insurance policies issued by other companies in connection with these pending audits. The Company does not consider the amount of this reserve to be material to the Company's financial condition or results of operations. With respect to one block of life insurance policies that is co-insured by a subsidiary of the Company, the Company is presently unable to estimate the reasonably possible loss or range of loss due to a number of factors, including uncertainty as to the legal theory or theories that may give rise to liability, uncertainty as to whether the Company or other companies are responsible for the liabilities, if any, arising in connection with such policies, the distinct characteristics of this co-insured block of policies which differentiate it from the blocks of life insurance policies for which the Company has recorded a reserve, and the early stages of the audits being conducted. The Company will continue to monitor the matter for any developments that would make the loss contingency associated with this block of co-insured policies probable or reasonably estimable.

Certain of the Company's subsidiaries have received notice that they are subject to a targeted multi-state examination with respect to their claims paying practices and their use of the U.S. Social Security Administration's Death Master File or similar databases (a "Death Database") to identify unreported deaths in their life insurance policies, annuity contracts and retained asset accounts. There is no clear basis in previously existing law for requiring a life insurer to search for unreported deaths in order to determine whether a benefit is owed, and substantial legal authority exists to support the position that the prevailing industry practice was lawful. A number of life insurers, however, have entered into settlement or consent agreements with state insurance regulators under which the life insurers agreed to implement procedures for periodically comparing their life insurance and annuity contracts and retained asset accounts against a Death Database, treating confirmed deaths as giving rise to a death benefit under their policies, locating beneficiaries and paying them the benefits and interest, and escheating the benefits and interest as well as penalties to the state if the beneficiary could not be found. It has been publicly reported that the life insurers have paid substantial administrative and/or examination fees to the insurance regulators in connection with the settlement or consent agreements. The Company believes it is reasonably possible that insurance regulators could demand from the Company administrative and/or examination fees relating to the targeted multi-state examination. Based on publicly reported payments by other life insurers, the Company estimates the range of such fees to be from \$0 to \$3.5 million.





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During the six months ended June 30, 2014, 203,295 performance shares with an estimated fair value of \$10.5 million were awarded. The criteria for payment of the 2014 performance awards is based primarily on the Company's average operating return on average equity ( ROE ) over a three-year period. If the Company's ROE is below 10.5%, no award is earned. If the Company's ROE is at or above 12.0%, the award maximum is earned. Awards are paid in shares of the Company's common stock.

Restricted stock units are awarded to participants and include certain restrictions relating to vesting periods. The Company issued 98,700 restricted stock units for the six months ended June 30, 2014. These awards had a total fair value at grant date of \$5.1 million. Approximately half of these restricted stock units vest after three years from the grant date and the remainder vest after four years.

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

|                              | Weighted-Average<br>Base Price per share | No. of SARs |
|------------------------------|--|-------------|
| Balance at December 31, 2013 | \$ 23.08                                 | 1,305,101   |
| SARs granted                 |  |             |
| SARs exercised / forfeited   | 26.43                                    | (62,167)    |
| Balance at June 30, 2014     | \$ 22.91                                 | 1,242,934   |

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. There were no SARs issued for the six months ended June 30, 2014.

For more information about the impact that the proposed merger with Dai-ichi will have on stock-based compensation, refer to Note 5, *Proposed Dai-ichi Merger*.

**12. EMPLOYEE BENEFIT PLANS**

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



|   |    |         |    |         |    |         |    |         |
|---|----|---------|----|---------|----|---------|----|---------|
| Service cost                                  |    |         |    |         |    |         |    |         |
| benefits earned                               |    |         |    |         |    |         |    |         |
| during the period                             | \$ | 2,453   | \$ | 2,708   | \$ | 4,906   | \$ | 5,416   |
| Interest cost on projected benefit obligation |    | 2,993   |    | 2,553   |    | 5,986   |    | 5,106   |
| Expected return on plan assets                |    | (3,065) |    | (2,759) |    | (6,130) |    | (5,518) |
| Amortization of prior service cost/(credit)   |    | (95)    |    | (95)    |    | (190)   |    | (190)   |
| Amortization of actuarial losses              |    | 1,897   |    | 2,729   |    | 3,794   |    | 5,458   |
| Total benefit cost                            | \$ | 4,183   | \$ | 5,136   | \$ | 8,366   | \$ | 10,272  |

During the six months ended June 30, 2014, the Company contributed \$2.3 million to its defined benefit pension plan for the 2013 plan year and \$3.1 million for the 2014 plan year. During July of 2014, the Company contributed \$3.1 million to the defined benefit pension plan for the 2014 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

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make additional contributions in future periods to maintain an adjusted funding target attainment percentage ( AFTAP ) of at least 80% and to avoid certain Pension Benefit Guaranty Corporation ( PBGC ) reporting triggers.

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 six months ended June 30, 2014, was immaterial to the Company's financial statements.

**13. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)**

The following tables summarize the changes in the accumulated balances for each component of accumulated other comprehensive income (loss) ( AOCI ) as of June 30, 2014 and December 31, 2013.

**Changes in Accumulated Other Comprehensive Income (Loss) by Component**

|  | Unrealized<br>Gains and Losses<br>on Investments(2) | Accumulated<br>Gain and Loss<br>Derivatives | Postretirement<br>Benefits Liability<br>Adjustment | Total<br>Accumulated<br>Other<br>Comprehensive<br>Income (Loss) |
|--|---|---|--|---|
|  | (Dollars In Thousands, Net of Tax)                  |   |  |   |
| <b>Beginning Balance, December 31, 2013</b>  | \$ 539,003  | \$ (1,235)                                  | \$ (43,702)  | \$ 494,066  |
| Other comprehensive income (loss) before reclassifications   | 884,120   | (17)  |  | 884,103   |
| Other comprehensive income (loss) relating to other- than-temporary impaired investments for which a portion has been recognized in earnings | 3,450   |   |  | 3,450   |
| Amounts reclassified from accumulated other comprehensive income (loss)(1)   | (15,936)  | 835   | 2,347  | (12,754)  |
| <b>Net current-period other comprehensive income</b>   | 871,634   | 818   | 2,347  | 874,799   |
| <b>Ending Balance, June 30, 2014</b>   | \$ 1,410,637  | \$ (417)                                    | \$ (41,355)  | \$ 1,368,865  |

(1) See Reclassification table below for details.

(2) These balances were offset by the impact of DAC and VOBA by \$198.1 million and \$413.4 million as of December 31, 2013 and June 30, 2014, respectively.

**Changes in Accumulated Other Comprehensive Income (Loss) by Component**

|  | Unrealized<br>Gains and Losses<br>on Investments(2) | Accumulated<br>Gain and Loss<br>Derivatives | Postretirement<br>Benefits Liability<br>Adjustment | Total<br>Accumulated<br>Other<br>Comprehensive<br>Income (Loss) |
|--|---|---|--|---|
|  | (Dollars In Thousands, Net of Tax)                  |   |  |   |
| <b>Beginning Balance, December 31, 2012</b>  | \$ 1,813,516  | \$ (3,496)                                  | \$ (73,298)  | \$ 1,736,722  |
| Other comprehensive income (loss) before reclassifications   | (1,250,498)   | 734   | 29,596   | (1,220,168)   |
| Other comprehensive income (loss) relating to other- than-temporary impaired investments for which a portion has been recognized in earnings | 4,591   |   |  | 4,591   |
| Amounts reclassified from accumulated other comprehensive income (loss)(1)   | (28,606)  | 1,527                                       |  | (27,079)  |
| <b>Net current-period other comprehensive income (loss)</b>  | <b>(1,274,513)</b>                                  | <b>2,261</b>                                | <b>29,596</b>                                      | <b>(1,242,656)</b>  |
| <b>Ending Balance, December 31, 2013</b>   | <b>\$ 539,003</b>                                   | <b>\$ (1,235)</b>                           | <b>\$ (43,702)</b>                                 | <b>\$ 494,066</b>   |

(1) See Reclassification table below for details.

(2) These balances were offset by the impact of DAC and VOBA by \$204.9 million and \$198.1 million as of December 31, 2012 and December 31, 2013, respectively.

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The following tables summarize the reclassifications amounts out of AOCI for the three months ended June 30, 2014 and 2013.

**Reclassifications Out of Accumulated Other Comprehensive Income (Loss)**

|   | <b>Amount<br/>Reclassified<br/>from Accumulated<br/>Other Comprehensive<br/>Income (Loss)<br/>(Dollars In Thousands)</b> | <b>Affected Line Item in the<br/>Consolidated Condensed Statements of Income</b> |
|---|--|--|
| <b>For The Three Months Ended June 30, 2014</b>                     |  |  |
| <b>Gains and losses on derivative instruments</b>                   |  |  |
| Net settlement (expense)/benefit(1)                                 | \$ (614)   | Benefits and settlement expenses, net of reinsurance ceded                       |
|   |  | (614) Total before tax   |
|   |  | 215 Tax (expense) or benefit   |
|   | \$ (399)   | Net of tax   |
| <b>Unrealized gains and losses on available-for-sale securities</b> |  |  |
| Net investment gains/losses   | \$ 20,198  | Realized investment gains (losses): All other investments                        |
| Impairments recognized in earnings                                  | (1,460)  | Net impairment losses recognized in earnings                                     |
|   |  | 18,738 Total before tax  |
|   |  | (6,558) Tax (expense) or benefit   |
|   | \$ 12,180  | Net of tax   |
| <b>Postretirement benefits liability adjustment</b>                 |  |  |
| Amortization of net actuarial gain/(loss)                           | \$ (1,900)   | Other operating expenses   |
| Amortization of prior service credit/(cost)                         | 95   | Other operating expenses   |
|   |  | (1,805) Total before tax   |
|   |  | 632 Tax (expense) or benefit   |
|   | \$ (1,173)   | Net of tax   |

(1) See Note 17, Derivative Financial Instruments for additional information.

**Reclassifications Out of Accumulated Other Comprehensive Income (Loss)**

|   | <b>Amount<br/>Reclassified<br/>from Accumulated<br/>Other Comprehensive<br/>Income (Loss)<br/>(Dollars In Thousands)</b> | <b>Affected Line Item in the<br/>Consolidated Condensed Statements of Income</b> |
|---|--|--|
| <b>For The Three Months Ended June 30, 2013</b>   |  |  |
| <b>Gains and losses on derivative instruments</b> |  |  |

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|   |    |         |  |
|---|----|---------|--|
| Net settlement (expense)/benefit(1)                                 | \$ | (580)   | Benefits and settlement expenses, net of reinsurance ceded |
|   |    | (580)   | Total before tax   |
|   |    | 203     | Tax (expense) or benefit                                   |
|   | \$ | (377)   | Net of tax   |
| <b>Unrealized gains and losses on available-for-sale securities</b> |    |         |  |
| Net investment gains/losses   | \$ | 21,518  | Realized investment gains (losses): All other investments  |
| Impairments recognized in earnings                                  |    | (4,000) | Net impairment losses recognized in earnings               |
|   |    | 17,518  | Total before tax   |
|   |    | (6,131) | Tax (expense) or benefit                                   |
|   | \$ | 11,387  | Net of tax   |

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(1) See Note 17, Derivative Financial Instruments for additional information.

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The following tables summarize the reclassifications amounts out of AOCI for the six months ended June 30, 2014 and 2013.

**Reclassifications Out of Accumulated Other Comprehensive Income (Loss)**

|   | <b>Amount<br/>Reclassified<br/>from Accumulated<br/>Other Comprehensive<br/>Income (Loss)<br/>(Dollars In Thousands)</b> | <b>Affected Line Item in the<br/>Consolidated Condensed Statements of Income</b> |
|---|--|--|
| <b>For The Six Months Ended June 30, 2014</b>                       |  |  |
| <b>Gains and losses on derivative instruments</b>                   |  |  |
| Net settlement (expense)/benefit(1)                                 | \$ (1,284)   | Benefits and settlement expenses, net of reinsurance ceded                       |
|   | (1,284)  | Total before tax   |
|   | 449  | Tax (expense) or benefit   |
|   | \$ (835)   | Net of tax   |
| <b>Unrealized gains and losses on available-for-sale securities</b> |  |  |
| Net investment gains/losses   | \$ 27,568  | Realized investment gains (losses): All other investments                        |
| Impairments recognized in earnings                                  | (3,051)  | Net impairment losses recognized in earnings                                     |
|   | 24,517   | Total before tax   |
|   | (8,581)  | Tax (expense) or benefit   |
|   | \$ 15,936  | Net of tax   |
| <b>Postretirement benefits liability adjustment</b>                 |  |  |
| Amortization of net actuarial gain/(loss)                           | \$ (3,800)   | Other operating expenses   |
| Amortization of prior service credit/(cost)                         | 190  | Other operating expenses   |
|   | (3,610)  | Total before tax   |
|   | 1,263  | Tax (expense) or benefit   |
|   | \$ (2,347)   | Net of tax   |

(1) See Note 17, Derivative Financial Instruments for additional information.

**Reclassifications Out of Accumulated Other Comprehensive Income (Loss)**

|   | <b>Amount<br/>Reclassified<br/>from Accumulated<br/>Other Comprehensive<br/>Income (Loss)<br/>(Dollars In Thousands)</b> | <b>Affected Line Item in the<br/>Consolidated Condensed Statements of Income</b> |
|---|--|--|
| <b>For The Six Months Ended June 30, 2013</b>     |  |  |
| <b>Gains and losses on derivative instruments</b> |  |  |

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|   |    |         |  |
|---|----|---------|--|
| Net settlement (expense)/benefit(1)                                 | \$ | (1,077) | Benefits and settlement expenses, net of reinsurance ceded |
|   |    | (1,077) | Total before tax   |
|   |    | 377     | Tax (expense) or benefit                                   |
|   | \$ | (700)   | Net of tax   |
| <b>Unrealized gains and losses on available-for-sale securities</b> |    |         |  |
| Net investment gains/losses   | \$ | 33,828  | Realized investment gains (losses): All other investments  |
| Impairments recognized in earnings                                  |    | (8,584) | Net impairment losses recognized in earnings               |
|   |    | 25,244  | Total before tax   |
|   |    | (8,835) | Tax (expense) or benefit                                   |
|   | \$ | 16,409  | Net of tax   |

(1) See Note 17, Derivative Financial Instruments for additional information.



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Basic earnings per share is computed by dividing net income 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 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:

| <b>Calculation of basic earnings per share:</b>             |    |            |    |            |    |            |    |            |
|---|----|------------|----|------------|----|------------|----|------------|
| Net income  | \$ | 107,977    | \$ | 103,199    | \$ | 191,616    | \$ | 181,490    |
| Average shares issued and outstanding                       |    | 78,852,583 |    | 78,456,663 |    | 78,740,416 |    | 78,332,481 |
| Issuable under various deferred compensation plans          |    | 1,126,570  |    | 948,107    |    | 1,054,415  |    | 940,333    |
| Weighted shares outstanding - basic                         |    | 79,979,153 |    | 79,404,770 |    | 79,794,831 |    | 79,272,814 |
| Per share:  |    |            |    |            |    |            |    |            |
| Net income - basic  | \$ | 1.35       | \$ | 1.30       | \$ | 2.40       | \$ | 2.29       |
| <b>Calculation of diluted earnings per share:</b>           |    |            |    |            |    |            |    |            |
| Net income  | \$ | 107,977    | \$ | 103,199    | \$ | 191,616    | \$ | 181,490    |
| Weighted shares outstanding - basic                         |    | 79,979,153 |    | 79,404,770 |    | 79,794,831 |    | 79,272,814 |
| Stock appreciation rights ( SARs )(1)                       |    | 492,463    |    | 449,726    |    | 479,430    |    | 444,971    |
| Issuable under various other stock-based compensation plans |    | 716,327    |    | 874,019    |    | 641,411    |    | 843,554    |
| Restricted stock units                                      |    | 258,334    |    | 358,723    |    | 245,128    |    | 336,703    |
| Weighted shares outstanding - diluted                       |    | 81,446,277 |    | 81,087,238 |    | 81,160,800 |    | 80,898,042 |
| Per share:  |    |            |    |            |    |            |    |            |
| Net income - diluted  | \$ | 1.33       | \$ | 1.27       | \$ | 2.36       | \$ | 2.24       |

(1)Excludes 629,800 SARs as of June 30, 2013 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.

**15. INCOME TAXES**

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In the IRS audit that concluded in 2012, the IRS proposed favorable and unfavorable adjustments to the Company's 2003 through 2007 reported taxable incomes. The Company protested certain unfavorable adjustments and is seeking resolution at the IRS Appeals Division. If the IRS prevails at Appeals, and the Company does not litigate these issues, then an acceleration of tax payments will occur. However, such accelerated payments would not materially impact the Company or its effective tax rate.

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A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

|   | June 30, 2014          | As of<br>December 31, 2013 |
|---|------------------------|----------------------------|
|   | (Dollars In Thousands) |                            |
| Balance, beginning of period                    | \$ 105,881             | \$ 75,292                  |
| Additions for tax positions of the current year | 948                    | 7,465                      |
| Additions for tax positions of prior years      | 41,246                 | 26,386                     |
| Reductions of tax positions of prior years:     |                        |                            |
| Changes in judgment                             | (10,548)               | (2,740)                    |
| Settlements during the period                   |                        |                            |
| Lapses of applicable statute of limitations     |                        | (522)                      |
| Balance, end of period                          | \$ 137,527             | \$ 105,881                 |

The Company believes that it is possible that in the next 12 months approximately \$18.5 million of these unrecognized tax benefits will be reduced due to the expected closure of the aforementioned Appeals process. In general, this closure would represent the Company's possible successful negotiation of certain issues, coupled with its payment of the assessed taxes on the remaining issues. Regarding the amounts reported above for the six months ended June 30, 2014 and the twelve months ended December 31, 2013, discussions with the IRS during these periods, which related to their ongoing examination of tax years 2008 through 2011, prompted the Company to contemporaneously revise upward its measurement of unrecognized tax benefits. These revisions included increasing prior determinations of amounts accrued for in earlier years as well as reducing some previously accrued amounts. These changes were almost entirely related to timing issues. Therefore, aside from the cost of interest, such changes did not result in any impact on the Company's effective tax rate.

Subsequent to June 30, 2014, the Internal Revenue Service issued guidance related to the tax method of accounting for hedges of guaranteed benefits on variable annuity contracts. The Company has issued contracts that provide such benefits. It has treated the derivatives that economically hedge the risk associated with such contracts as tax hedges. There are several uncertainties regarding the provisions of this guidance. Examples include its effective date and its scope. Therefore, it is uncertain at this time whether this guidance will be applicable to the Company and whether it will adopt this guidance's prescribed methodology. Consequently, the Company currently believes that the amounts of unrecognized tax benefits that relate to this issue and that are disclosed above are appropriate.

The Company used its estimate of its annual 2014 and 2013 income in computing its effective income tax rates for the three and six months ended June 30, 2014 and 2013. The effective tax rates for the three and six months ended June 30, 2014 were 33.4% and 33.3%, respectively, and 34.3% and 33.9% for the three and six months ended June 30, 2013, respectively.

In general, the Company is no longer subject to U.S. federal, state, and local income tax examinations by taxing authorities for tax years that began before 2003.

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 June 30, 2014.



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**16. FAIR VALUE OF FINANCIAL INSTRUMENTS**

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

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

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The following table presents the Company's hierarchy for its assets and liabilities measured at fair value on a recurring basis as of June 30, 2014:

| <b>Assets:</b>  |               |    |              |              |               |
|---|---------------|----|--------------|--------------|---------------|
| Fixed maturity securities - available-for-sale                |               |    |              |              |               |
| Residential mortgage-backed securities                        | \$            |    | \$ 1,434,727 | \$ 10        | \$ 1,434,737  |
| Commercial mortgage-backed securities                         |               |    | 1,087,615    |              | 1,087,615     |
| Other asset-backed securities                                 |               |    | 297,588      | 568,097      | 865,685       |
| U.S. government-related securities                            | 1,295,535     |    | 273,196      |              | 1,568,731     |
| State, municipalities, and political subdivisions             |               |    | 1,599,174    | 3,675        | 1,602,849     |
| Other government-related securities                           |               |    | 22,214       |              | 22,214        |
| Corporate bonds   | 132           |    | 26,203,478   | 1,524,297    | 27,727,907    |
| Total fixed maturity securities - available-for-sale          | 1,295,667     |    | 30,917,992   | 2,096,079    | 34,309,738    |
| Fixed maturity securities - trading                           |               |    |              |              |               |
| Residential mortgage-backed securities                        |               |    | 298,684      | 842          | 299,526       |
| Commercial mortgage-backed securities                         |               |    | 159,899      |              | 159,899       |
| Other asset-backed securities                                 |               |    | 95,012       | 176,386      | 271,398       |
| U.S. government-related securities                            | 212,167       |    | 4,948        |              | 217,115       |
| State, municipalities, and political subdivisions             |               |    | 281,182      |              | 281,182       |
| Other government-related securities                           |               |    | 56,142       |              | 56,142        |
| Corporate bonds   |               |    | 1,537,907    | 31,520       | 1,569,427     |
| Total fixed maturity securities - trading                     | 212,167       |    | 2,433,774    | 208,748      | 2,854,689     |
| Total fixed maturity securities                               | 1,507,834     |    | 33,351,766   | 2,304,827    | 37,164,427    |
| Equity securities   | 621,868       |    | 88,395       | 81,784       | 792,047       |
| Other long-term investments(1)                                | 78,391        |    | 64,075       | 123,301      | 265,767       |
| Short-term investments  | 202,443       |    | 6,181        |              | 208,624       |
| Total investments   | 2,410,536     |    | 33,510,417   | 2,509,912    | 38,430,865    |
| Cash  | 361,088       |    |              |              | 361,088       |
| Other assets  | 11,692        |    |              |              | 11,692        |
| Assets related to separate accounts                           |               |    |              |              |               |
| Variable annuity  | 13,304,455    |    |              |              | 13,304,455    |
| Variable universal life                                       | 823,747       |    |              |              | 823,747       |
| Total assets measured at fair value on a recurring basis      | \$ 16,911,518 | \$ | 33,510,417   | \$ 2,509,912 | \$ 52,931,847 |
| <b>Liabilities:</b>   |               |    |              |              |               |
| Annuity account balances(2)                                   | \$            | \$ |              | \$ 102,456   | \$ 102,456    |
| Other liabilities (1)   | 36,608        |    | 64,374       | 484,747      | 585,729       |
| Total liabilities measured at fair value on a recurring basis | \$ 36,608     | \$ | 64,374       | \$ 587,203   | \$ 688,185    |

(1)Includes certain freestanding and embedded derivatives.

(2)Represents liabilities related to fixed indexed annuities.



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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, 2013:

| <b>Assets:</b>  |               |               |              |               |              |
|---|---------------|---------------|--------------|---------------|--------------|
| Fixed maturity securities - available-for-sale                |               |               |              |               |              |
| Residential mortgage-backed securities                        | \$            |               | \$ 1,445,040 | \$ 28         | \$ 1,445,068 |
| Commercial mortgage-backed securities                         |               |               | 970,656      |               | 970,656      |
| Other asset-backed securities                                 |               |               | 326,175      | 545,808       | 871,983      |
| U.S. government-related securities                            | 1,211,141     |               | 296,749      |               | 1,507,890    |
| State, municipalities, and political subdivisions             |               |               | 1,407,154    | 3,675         | 1,410,829    |
| Other government-related securities                           |               |               | 51,427       |               | 51,427       |
| Corporate bonds   | 107           |               | 24,209,541   | 1,549,940     | 25,759,588   |
| Total fixed maturity securities - available-for-sale          | 1,211,248     |               | 28,706,742   | 2,099,451     | 32,017,441   |
| Fixed maturity securities - trading                           |               |               |              |               |              |
| Residential mortgage-backed securities                        |               |               | 310,877      |               | 310,877      |
| Commercial mortgage-backed securities                         |               |               | 158,570      |               | 158,570      |
| Other asset-backed securities                                 |               |               | 93,278       | 194,977       | 288,255      |
| U.S. government-related securities                            | 191,332       |               | 4,906        |               | 196,238      |
| State, municipalities, and political subdivisions             |               |               | 260,892      |               | 260,892      |
| Other government-related securities                           |               |               | 57,097       |               | 57,097       |
| Corporate bonds   |               |               | 1,497,362    | 29,199        | 1,526,561    |
| Total fixed maturity securities - trading                     | 191,332       |               | 2,382,982    | 224,176       | 2,798,490    |
| Total fixed maturity securities                               | 1,402,580     |               | 31,089,724   | 2,323,627     | 34,815,931   |
| Equity securities   | 523,219       |               | 50,927       | 71,881        | 646,027      |
| Other long-term investments (1)                               | 56,469        |               | 54,965       | 196,133       | 307,567      |
| Short-term investments  | 132,543       |               | 1,603        |               | 134,146      |
| Total investments   | 2,114,811     |               | 31,197,219   | 2,591,641     | 35,903,671   |
| Cash  | 466,542       |               |              |               | 466,542      |
| Other assets  | 10,979        |               |              |               | 10,979       |
| Assets related to separate accounts                           |               |               |              |               |              |
| Variable annuity  | 12,791,438    |               |              |               | 12,791,438   |
| Variable universal life                                       | 783,618       |               |              |               | 783,618      |
| Total assets measured at fair value on a recurring basis      | \$ 16,167,388 | \$ 31,197,219 | \$ 2,591,641 | \$ 49,956,248 |              |
| <b>Liabilities:</b>   |               |               |              |               |              |
| Annuity account balances (2)                                  | \$            | \$            | \$ 107,000   | \$            | 107,000      |
| Other liabilities (1)   | 30,241        | 156,931       | 270,630      | 457,802       |              |
| Total liabilities measured at fair value on a recurring basis | \$ 30,241     | \$ 156,931    | \$ 377,630   | \$ 564,802    |              |

(1)Includes certain freestanding and embedded derivatives.

(2)Represents liabilities related to fixed 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

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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 approximately 90% of the Company's available-for-sale and trading fixed maturity securities. Based on the typical trading volumes and the lack of quoted market prices for available-for-sale and trading 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 six months ended June 30, 2014.

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

*Asset-Backed Securities*

This category mainly consists of residential mortgage-backed securities, commercial mortgage-backed securities, and other asset-backed securities (collectively referred to as asset-backed securities or ABS). As of June 30, 2014, the Company held \$3.4 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.

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

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discount margin. The Company reviews the methodologies and valuation techniques (including the ability to observe inputs) in assessing the information received from external pricing services and in consideration of the fair value presentation.

As of June 30, 2014, the Company held \$745.3 million of Level 3 ABS, which included \$568.1 million of other asset-backed securities classified as available-for-sale and \$177.2 million of other asset-backed classified as trading. These securities are predominantly ARS whose underlying collateral is at least 97% guaranteed by the FFELP. As a result of the ARS market collapse during 2008, the Company prices its ARS using an income approach valuation model. As part of the valuation process the Company reviews the following characteristics of the ARS in determining the relevant inputs: 1) weighted-average coupon rate, 2) weighted-average years to maturity, 3) types of underlying assets, 4) weighted-average coupon rate of the underlying assets, 5) weighted-average years to maturity of the underlying assets, 6) seniority level of the tranches owned, 7) credit ratings of the securities, 8) liquidity premium, and 9) paydown rate.

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

As of June 30, 2014, the Company classified approximately \$30.0 billion of corporate bonds, U.S. government-related securities, states, municipals, and political subdivisions, and other government-related securities as Level 2. The fair value of the Level 2 bonds and securities is predominantly priced by broker quotes and a third party pricing service. The Company has reviewed the valuation techniques of the brokers and third party pricing service and has determined that such techniques used Level 2 market observable inputs. The following characteristics of the bonds and securities are considered to be the primary relevant inputs to the valuation: 1) weighted- average coupon rate, 2) weighted-average years to maturity, 3) seniority, and 4) credit ratings. The Company reviews the methodologies and valuation techniques (including the ability to observe inputs) in assessing the information received from external pricing services and in consideration of the fair value presentation.

The brokers and third party pricing service utilize valuation models that consist of a hybrid income and market approach to valuation. The pricing models utilize 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 June 30, 2014, the Company classified approximately \$1.6 billion of bonds and securities as Level 3 valuations. Level 3 bonds and securities primarily represent investments in illiquid bonds for which no price is readily available. To determine a price, the Company uses a discounted cash flow model with both observable and unobservable inputs. These inputs are entered into an industry standard pricing model to determine the final price of the security. These inputs include: 1) principal and interest payments, 2) coupon rate, 3) sector and issuer level spread over treasury, 4) underlying collateral, 5) credit ratings, 6) maturity, 7) embedded options, 8) recent new issuance, 9) comparative bond analysis, and 10) an illiquidity premium.

***Equities***

As of June 30, 2014, the Company held approximately \$170.2 million of equity securities classified as Level 2 and Level 3. Of this total, \$66.4 million represents Federal Home Loan Bank ( FHLB ) stock. The Company believes that the cost of the FHLB stock approximates fair value. The remainder of these equity securities is primarily investments in preferred stock.

*Other long-term investments and other liabilities*

Other long-term investments and other liabilities consist entirely of free-standing and embedded derivative financial instruments. Refer to Note 17, *Derivative Financial Instruments* for additional information related to derivatives. Derivative financial instruments are valued using exchange prices, independent broker quotations, or pricing valuation models, which utilize market data inputs. Excluding embedded derivatives, as of June 30, 2014, 96.6% 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

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data inputs. Inputs used to value derivatives include, but are not limited to, interest swap rates, credit spreads, interest rate and equity market volatility indices, equity index levels, and treasury rates. The Company performs monthly analysis on derivative valuations that includes both quantitative and qualitative analyses.

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

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

Derivative instruments classified as Level 3 were embedded derivatives and include at least one significant non-observable 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 embedded derivatives are carried at fair value in other long-term investments and other liabilities on the Company's consolidated balance sheet. The changes in fair value are recorded in earnings as Realized investment gains (losses) Derivative financial instruments. Refer to Note 17, *Derivative Financial Instruments* for more information related to each embedded derivatives gains and losses.

The fair value of the guaranteed minimum withdrawal benefits (GMWB) embedded derivative is derived through the income method of valuation using a valuation model that projects future cash flows using multiple risk neutral stochastic equity scenarios and policyholder behavior assumptions. The risk neutral scenarios are generated using the current swap curve and projected equity volatilities and correlations. The projected equity volatilities are based on a blend of historical volatility and near-term equity market implied volatilities. The equity correlations are based on historical price observations. For policyholder behavior assumptions, expected lapse and utilization assumptions are used and updated for actual experience, as necessary. The Company assumes age-based mortality from the National Association of Insurance Commissioners 1994 Variable Annuity MGDB Mortality Table for company experience, with attained age factors varying from 49% - 80%. The present value of the cash flows is determined using the discount rate curve, which is based upon LIBOR plus a credit spread (to represent the Company's non-performance risk). As a result of using significant unobservable inputs, the GMWB embedded derivative is categorized as Level 3. These assumptions are reviewed on a quarterly basis.

The balance of the fixed indexed annuities (FIA) embedded derivative is impacted by policyholder cash flows associated with the FIA product that are allocated to the embedded derivative in addition to changes in the fair value of the embedded derivative during the reporting period. The fair value of the FIA embedded derivative is derived through the income method of valuation using a valuation model that projects future cash flows using current index values and volatility, the hedge budget used to price the product, and policyholder assumptions (both elective and non-elective). For policyholder behavior assumptions, expected lapse and withdrawal assumptions are used and updated for actual experience, as necessary. The Company assumes age-based mortality from the 1994 Variable Annuity MGDB mortality table modified for company experience, with attained age factors varying from 49% - 80%. The present value of the cash flows is determined using the discount rate curve,

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which is based upon LIBOR up to one year and constant maturity treasury rates plus a credit spread (to represent the Company's non-performance risk) thereafter. Policyholder assumptions are reviewed on an annual basis. As a result of using significant unobservable inputs, the FIA embedded derivative is categorized as Level 3.

The balance of the indexed universal life ( IUL ) embedded derivative is impacted by policyholder cash flows associated with the IUL product that are allocated to the embedded derivative in addition to changes in the fair value of the embedded derivative during the reporting period. The fair value of the IUL embedded derivative is derived through the income method of valuation using a valuation model that projects future cash flows using current index values and volatility, the hedge budget used to price the product, and policyholder assumptions (both elective and non-elective).

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For policyholder behavior assumptions, expected lapse and withdrawal assumptions are used and updated for actual experience, as necessary. The Company assumes age-based mortality from the SOA 2008 VBT Primary Tables modified for company experience, with attained age factors varying from 37% - 74%. The present value of the cash flows is determined using the discount rate curve, which is based upon LIBOR up to one year and constant maturity treasury rates plus a credit spread (to represent the Company's non-performance risk) thereafter. Policyholder assumptions are reviewed on an annual basis. As a result of using significant unobservable inputs, the IUL embedded derivative is categorized as Level 3.

The Company has assumed and ceded certain blocks of policies under modified coinsurance agreements in which the investment results of the underlying portfolios inure directly to the reinsurers. As a result, these agreements contain embedded derivatives that are reported at fair value. Changes in their fair value are reported in earnings. The investments supporting these agreements are designated as trading securities; therefore changes in their fair value are also reported in earnings. The fair value of the embedded derivative is the difference between the statutory policy liabilities (net of policy loans) of \$2.6 billion and the fair value of the trading securities of \$2.9 billion. As a result, changes in the fair value of the embedded derivatives are largely offset by the changes in fair value of the related investments and each are reported in earnings. The fair value of the embedded derivative is considered a Level 3 valuation due to the unobservable nature of the policy liabilities.

*Annuity account balances*

The Company records certain of its FIA reserves at fair value. The fair value is considered a Level 3 valuation. The FIA valuation model calculates the present value of future benefit cash flows less the projected future profits to quantify the net liability that is held as a reserve. This calculation is done using multiple risk neutral stochastic equity scenarios. The cash flows are discounted using LIBOR plus a credit spread. Best estimate assumptions are used for partial withdrawals, lapses, expenses and asset earned rate with a risk margin applied to each. These assumptions are reviewed at least annually as a part of the formal unlocking process. If an event were to occur within a quarter that would make the assumptions unreasonable, the assumptions would be reviewed within the quarter.

The discount rate for the fixed indexed annuities is based on an upward sloping rate curve which is updated each quarter. The discount rates for June 30, 2014, ranged from a one month rate of 0.26%, a 5 year rate of 2.24%, and a 30 year rate of 4.24%. A credit spread component is also included in the calculation to accommodate non-performance risk.

*Separate Accounts*

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



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*Valuation of Level 3 Financial Instruments*

The following table presents the valuation method for material financial instruments included in Level 3, as well as the unobservable inputs used in the valuation of those financial instruments:

| <b>Assets:</b>            |           |                           |                          |   |
|---------------------------|-----------|---------------------------|--------------------------|---|
| Corporate bonds           | 1,461,997 | Discounted cash flow      | Spread over treasury     | 0.06% - 6.90% (1.88%)                                       |
| <b>Liabilities:</b>       |           |                           |                          |   |
| Embedded derivative - FIA | 69,615    | Actuarial cash flow model | Expenses Withdrawal rate | \$83 - \$97 per policy<br>1.1% - 4.5% depending on duration |



(1)The fair value for the GMWB embedded derivative is presented as a net asset for the purposes of this chart. Excludes modified coinsurance arrangements.

(2)Represents liabilities related to fixed indexed annuities.

The chart above excludes Level 3 financial instruments that are valued using broker quotes and those which book value approximates fair value.

The Company has considered all reasonably available quantitative inputs as of June 30, 2014, but the valuation techniques and inputs used by some brokers in pricing certain financial instruments are not shared with the Company. This resulted in \$263.0 million of financial instruments being classified as Level 3 as of June 30, 2014. Of the \$263.0 million, \$177.8 million are other asset-backed securities, \$73.9 million are corporate bonds, and \$11.3 million are equity securities.

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In certain cases the Company has determined that book value materially approximates fair value. As of June 30, 2014, the Company held \$94.1 million of financial instruments where book value approximates fair value. Of the \$94.1 million, \$70.5 million represents equity securities, which are predominantly FHLB stock, \$19.9 million are corporate bonds, and \$3.7 million of other fixed maturity securities.

The following table presents the valuation method for material financial instruments included in Level 3, as well as the unobservable inputs used in the valuation of those financial instruments:

| Assets:                   |           |                           |                          |   |
|---------------------------|-----------|---------------------------|--------------------------|---|
|                           |           |                           |                          |   |
| Corporate bonds           | 1,555,898 | Discounted cash flow      | Spread over treasury     | 0.11% - 6.75% (2.06%)   |
|                           |           |                           |                          |   |
|                           |           |                           |                          |   |
| Liabilities:              |           |                           |                          |   |
|                           |           |                           |                          |   |
|                           |           |                           |                          |   |
|                           |           |                           |                          |   |
| Embedded derivative - FIA | 25,324    | Actuarial cash flow model | Expenses Withdrawal rate | \$83 - \$97 per policy<br>1.1% - 4.5% depending on duration and tax qualification |

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|  |                     |   |
|--|---------------------|---|
|  |                     | 49% to 80% of 1994 MGDB table                               |
|  | Mortality           | 2.5% - 40.0%, depending on duration/surrender charge period |
|  | Lapse               | 0.15% - 1.06%   |
|  | Nonperformance risk |   |

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(1)The fair value for the GMWB embedded derivative is presented as a net asset for the purposes of this chart. Excludes modified coinsurance arrangements.

(2)Represents liabilities related to fixed indexed annuities.

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The chart above excludes Level 3 financial instruments that are valued using broker quotes and those which book value approximates fair value.

The Company has considered all reasonably available quantitative inputs as of December 31, 2013, but the valuation techniques and inputs used by some brokers in pricing certain financial instruments are not shared with the Company. This resulted in \$216.6 million of financial instruments being classified as Level 3 as of December 31, 2013. Of the \$216.6 million, \$195.0 million are other asset backed securities, \$21.0 million are corporate bonds, and \$0.6 million are equity securities.

In certain cases the Company has determined that book value materially approximates fair value. As of December 31, 2013, the Company held \$77.2 million of financial instruments where book value approximates fair value. Of the \$77.2 million, \$71.3 million represents equity securities, which are predominantly FHLB stock, \$2.2 million of other corporate bonds, and \$3.7 million of other fixed maturity securities.

The asset-backed securities classified as Level 3 are predominantly ARS. A change in the paydown rate (the projected annual rate of principal reduction) of the ARS can significantly impact the fair value of these securities. A decrease in the paydown rate would increase the projected weighted average life of the ARS and increase the sensitivity of the ARS fair value to changes in interest rates. An increase in the liquidity premium would result in a decrease in the fair value of the securities, while a decrease in the liquidity premium would increase the fair value of these securities.

The fair value of corporate bonds classified as Level 3 is sensitive to changes in the interest rate spread over the corresponding U.S. Treasury rate. This spread represents a risk premium that is impacted by company specific and market factors. An increase in the spread can be caused by a perceived increase in credit risk of a specific issuer and/or an increase in the overall market risk premium associated with similar securities. The fair values of corporate bonds are sensitive to changes in spread. When holding the treasury rate constant, the fair value of corporate bonds increase when spreads decrease, and decrease when spreads increase.

The fair value of the GMWB embedded derivative is sensitive to changes in the discount rate which includes the Company's nonperformance risk, volatility, lapse, and mortality assumptions. The volatility assumption is an observable input as it is based on market inputs. The Company's nonperformance risk, lapse, and mortality are unobservable. An increase in the three unobservable assumptions would result in a decrease in the fair value and conversely, if there is a decrease in the assumptions the fair value would increase. The fair value is also dependent on the assumed policyholder utilization of the GMWB where an increase in assumed utilization would result in an increase in the fair value and conversely, if there is a decrease in the assumption, the fair value would decrease.

The fair value of the FIA account balance liability is predominantly impacted by observable inputs such as discount rates and equity returns. However, the fair value of the FIA account balance liability is sensitive to the asset earned rate and required return on assets. The value of the liability increases with an increase in required return on assets and a decrease in the asset earned rate and conversely, the value of the liability decreases with a decrease in required return on assets and an increase in the asset earned rate.

The fair value of the FIA embedded derivative is predominantly impacted by observable inputs such as discount rates and equity returns. However, the fair value of the FIA embedded derivative is sensitive to non-performance risk. The value of the liability increases with decreases in the discount rate and non-performance risk and decreases with increases in the discount rate and nonperformance risk. The value of the liability increases with increases in equity returns and the liability decreases with a decrease in equity returns.

The fair value of the IUL embedded derivative is predominantly impacted by observable inputs such as discount rates and equity returns. However, the fair value of the IUL embedded derivative is sensitive to non-performance risk. The value of the liability increases with decreases in the discount rate and non-performance risk and decreases with increases in the discount rate and nonperformance risk. The value of the liability increases with increases in equity returns and the liability decreases with a decrease in equity returns.

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The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the three months ended June 30, 2014, for which the Company has used significant unobservable inputs (Level 3):

| Assets:  |    |           |    |        |    |         |        |          |    |          |         |    |           |    |
|--|----|-----------|----|--------|----|---------|--------|----------|----|----------|---------|----|-----------|----|
| Residential mortgage-backed securities         | \$ | 17        | \$ | \$     | \$ | \$      | \$     | (7)      | \$ | \$       | \$      | \$ | 10        | \$ |
| Other asset-backed securities                  |    | 548,805   |    | 29,929 |    | (104)   |        | (9,534)  |    |          | (999)   |    | 568,097   |    |
| States, municipals, and political subdivisions |    | 3,675     |    |        |    |         |        |          |    |          |         |    | 3,675     |    |
| Corporate bonds                                |    | 1,573,710 | 74 | 27,271 |    | (2,250) | 60,845 | (65,172) |    | (67,478) | (2,703) |    | 1,524,297 |    |
| Fixed maturity securities - trading            |    |           |    |        |    |         |        |          |    |          |         |    |           |    |
| Commercial mortgage-backed securities          |    |           |    |        |    |         |        |          |    |          |         |    |           |    |
| U.S. government-related securities             |    |           |    |        |    |         |        |          |    |          |         |    |           |    |

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|   |              |          |              |             |            |           |              |             |            |              |              |
|---|--------------|----------|--------------|-------------|------------|-----------|--------------|-------------|------------|--------------|--------------|
| Other government-related securities                           |              |          |              |             |            |           |              |             |            |              |              |
| Total fixed maturity securities - trading                     | 225,610      | 6,464    | (2,726)      | 4,901       | (26,930)   | 1,250     | 179          | 208,748     | 802        |              |              |
| Equity securities   | 81,493       | 965      |              |             | (674)      |           |              | 81,784      |            |              |              |
| Short-term investments  |              |          |              |             |            |           |              |             |            |              |              |
| Total assets measured at fair value on a recurring basis      |              |          |              |             |            |           |              |             |            |              |              |
|   | \$ 2,577,118 | \$ 6,778 | \$ 58,165    | \$ (23,473) | \$ (2,354) | \$ 65,746 | \$ (102,317) | \$ (66,228) | \$ (3,523) | \$ 2,509,912 | \$ (19,705)  |
| Annuity account balances(2)                                   | \$ 105,593   | \$       | \$ (1,714)   | \$          | \$         | \$ 63     | \$ 4,914     | \$          | \$         | \$ 102,456   | \$           |
| Total liabilities measured at fair value on a recurring basis |              |          |              |             |            |           |              |             |            |              |              |
|   | \$ 476,958   | \$ 13    | \$ (115,109) | \$          | \$         | \$ 63     | \$ 4,914     | \$          | \$         | \$ 587,203   | \$ (113,382) |

(1)Represents certain freestanding and embedded derivatives.

(2)Represents liabilities related to fixed indexed annuities.

For the three months ended June 30, 2014, \$1.3 million of securities were transferred into Level 3. This amount was transferred from Level 2. These transfers resulted from securities that were priced by independent pricing services or brokers in previous periods, using no significant unobservable inputs, but were priced internally using significant unobservable inputs where market observable inputs were no longer available as of June 30, 2014.

For the three months ended June 30, 2014, \$67.5 million of securities were transferred into Level 2. This amount was transferred from Level 3. These transfers resulted from securities that were previously priced internally using significant unobservable inputs, now being priced by independent pricing services or brokers.

For the three months ended June 30, 2014, there were no transfers from Level 2 to Level 1.

For the three months ended June 30, 2014, there were no transfers from Level 1.



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The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the three months ended June 30, 2013, for which the Company has used significant unobservable inputs (Level 3):

| Assets:  |         |     |        |    |         |          |         |        |        |     |     |    |         |    |        |    |
|--|---------|-----|--------|----|---------|----------|---------|--------|--------|-----|-----|----|---------|----|--------|----|
| Residential mortgage-backed securities         | \$      | 4   | \$     | \$ | \$      | (337)    | \$      | 14,349 | \$     | \$  | \$  | 46 | \$      | \$ | 14,062 | \$ |
| Other asset-backed securities                  | 560,668 |     | 43,744 |    | 13,162  | (41,377) |         |        |        |     | 199 |    | 576,396 |    |        |    |
| States, municipals, and political subdivisions | 4,335   |     |        |    |         | (5)      |         |        |        |     |     |    | 4,330   |    |        |    |
| Corporate bonds                                | 124,555 | 116 | 81     |    | (7,682) | 18,275   | (3,113) |        | 62,330 | 333 |     |    | 194,895 |    |        |    |
| Fixed maturity securities - trading            |         |     |        |    |         |          |         |        |        |     |     |    |         |    |        |    |
| Commercial mortgage-backed securities          |         |     |        |    |         |          |         |        |        |     |     |    |         |    |        |    |
| U.S. government-related securities             |         |     |        |    |         |          |         |        |        |     |     |    |         |    |        |    |

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|   |            |            |             |            |            |            |             |           |          |              |            |
|---|------------|------------|-------------|------------|------------|------------|-------------|-----------|----------|--------------|------------|
| Other government-related securities                           |            |            |             |            |            |            |             |           |          |              |            |
| Total fixed maturity securities - trading                     | 76,495     | 1,389      | (2,633)     | 110,912    | (9,953)    | 2,210      | 605         | 179,025   | 488      |              |            |
| Equity securities   | 69,418     |            |             |            |            |            |             | 69,418    |          |              |            |
| Short-term investments  |            |            |             |            |            |            |             |           |          |              |            |
| Total assets measured at fair value on a recurring basis      |            |            |             |            |            |            |             |           |          |              |            |
|   | \$ 912,595 | \$ 44,822  | \$ 43,826   | \$ (2,995) | \$ (8,019) | \$ 156,698 | \$ (54,448) | \$ 64,586 | \$ 1,133 | \$ 1,158,198 | \$ 43,443  |
| Annuity account balances(2)                                   | \$ 123,681 | \$         | \$ (1,686)  | \$         | \$         | \$ 65      | \$ 10,818   | \$        | \$       | \$ 114,614   | \$         |
| Total liabilities measured at fair value on a recurring basis |            |            |             |            |            |            |             |           |          |              |            |
|   | \$ 663,495 | \$ 219,947 | \$ (17,400) | \$         | \$         | \$ 65      | \$ 10,818   | \$        | \$       | \$ 450,195   | \$ 204,233 |

(1)Represents certain freestanding and embedded derivatives.

(2)Represents liabilities related to fixed indexed annuities.

For the three months ended June 30, 2013, \$64.6 million of securities were transferred into Level 3. This amount was transferred from Level 2. These transfers resulted from securities that were priced by independent pricing services or brokers in previous periods, using no significant unobservable inputs, but were priced internally using significant unobservable inputs where market observable inputs were no longer available as of June 30, 2013. All transfers are recognized as of the end of the period.

For the three months ended June 30, 2013, there were no transfers out of Level 3.

For the three months ended June 30, 2013, there were no transfers from Level 2 to Level 1.

For the three months ended June 30, 2013, there were no transfers out of Level 1.

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The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the six months ended June 30, 2014, for which the Company has used significant unobservable inputs (Level 3):

| Assets:  |    |           |     |        |    |         |        |           |    |          |         |    |           |    |
|--|----|-----------|-----|--------|----|---------|--------|-----------|----|----------|---------|----|-----------|----|
| Residential mortgage-backed securities         | \$ | 28        | \$  | \$     | \$ | \$      | \$     | (18)      | \$ | \$       | \$      | \$ | 10        | \$ |
| Other asset-backed securities                  |    | 545,808   |     | 34,066 |    | (1,233) |        | (9,794)   |    |          | (750)   |    | 568,097   |    |
| States, municipals, and political subdivisions |    | 3,675     |     |        |    |         |        |           |    |          |         |    | 3,675     |    |
| Corporate bonds                                |    | 1,549,940 | 969 | 54,288 |    | (7,265) | 90,232 | (103,039) |    | (55,293) | (5,535) |    | 1,524,297 |    |
| Fixed maturity securities - trading            |    |           |     |        |    |         |        |           |    |          |         |    |           |    |
| Commercial mortgage-backed securities          |    |           |     |        |    |         |        |           |    |          |         |    |           |    |
| U.S. government-related securities             |    |           |     |        |    |         |        |           |    |          |         |    |           |    |

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|   |              |          |              |             |            |            |              |             |            |              |              |
|---|--------------|----------|--------------|-------------|------------|------------|--------------|-------------|------------|--------------|--------------|
| Other government-related securities                           |              |          |              |             |            |            |              |             |            |              |              |
| Total fixed maturity securities - trading                     | 224,176      | 7,729    | (3,167)      | 4,901       | (27,805)   | 2,522      | 392          | 208,748     | 654        |              |              |
| Equity securities   | 71,881       | 1,192    | (166)        | 9,551       | (674)      |            |              | 81,784      |            |              |              |
| Short-term investments  |              |          |              |             |            |            |              |             |            |              |              |
| Total assets measured at fair value on a recurring basis      |              |          |              |             |            |            |              |             |            |              |              |
|   | \$ 2,591,641 | \$ 8,943 | \$ 89,546    | \$ (76,244) | \$ (8,664) | \$ 104,684 | \$ (141,330) | \$ (52,771) | \$ (5,893) | \$ 2,509,912 | \$ (72,178)  |
| Annuity account balances(2)                                   | \$ 107,000   | \$       | \$ (3,123)   | \$          | \$         | \$ 175     | \$ 7,842     | \$          | \$         | \$ 102,456   | \$           |
| Total liabilities measured at fair value on a recurring basis |              |          |              |             |            |            |              |             |            |              |              |
|   | \$ 377,630   | \$ 25    | \$ (217,265) | \$          | \$         | \$ 175     | \$ 7,842     | \$          | \$         | \$ 587,203   | \$ (214,117) |

(1)Represents certain freestanding and embedded derivatives.

(2)Represents liabilities related to fixed indexed annuities.

For the six months ended June 30, 2014, \$31.0 million of securities were transferred into Level 3. This amount was transferred from Level 2. These transfers resulted from securities that were priced by independent pricing services or brokers in previous periods, using no significant unobservable inputs, but were priced internally using significant unobservable inputs where market observable inputs were no longer available as of June 30, 2014. All transfers are recognized as of the end of the period.

For the six months ended June 30, 2014, \$83.8 million of securities were transferred into Level 2. This amount was transferred from Level 3. These transfers resulted from securities that were previously priced internally using significant unobservable inputs, now being priced by independent pricing services or brokers.

For the six months ended June 30, 2014, there were no transfers from Level 2 to Level 1.

For the six months ended June 30, 2014, there were no transfers out of Level 1.

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The following table presents a reconciliation of the beginning and ending balances for fair value measurements for the six months ended June 30, 2013, for which the Company has used significant unobservable inputs (Level 3):

| Assets:  |         |     |        |    |          |        |          |        |        |     |         |    |    |    |        |
|--|---------|-----|--------|----|----------|--------|----------|--------|--------|-----|---------|----|----|----|--------|
| Residential mortgage-backed securities         | \$      | 4   | \$     | \$ | \$       | (337)  | \$       | 14,349 | \$     | \$  | \$      | 46 | \$ | \$ | 14,062 |
| Other asset-backed securities                  | 596,143 |     | 43,756 |    | (27,548) | 13,162 | (50,386) |        | 1,227  | 42  | 576,396 |    |    |    |        |
| States, municipals, and political subdivisions | 4,335   |     |        |    |          |        | (5)      |        |        |     | 4,330   |    |    |    |        |
| Corporate bonds                                | 167,892 | 116 | 1,011  |    | (10,046) | 18,275 | (45,184) |        | 62,330 | 501 | 194,895 |    |    |    |        |
| Fixed maturity securities - trading            |         |     |        |    |          |        |          |        |        |     |         |    |    |    |        |
| Commercial mortgage-backed securities          |         |     |        |    |          |        |          |        |        |     |         |    |    |    |        |
| U.S. government-related securities             |         |     |        |    |          |        |          |        |        |     |         |    |    |    |        |

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|   |            |            |             |            |             |            |              |         |           |            |              |           |
|---|------------|------------|-------------|------------|-------------|------------|--------------|---------|-----------|------------|--------------|-----------|
| Other government-related securities                           |            |            |             |            |             |            |              |         |           |            |              |           |
| Total fixed maturity securities - trading                     | 70,650     | 4,798      | (2,892)     | 110,912    | (12,793)    | 7,223      | 1,127        | 179,025 | 3,785     |            |              |           |
| Equity securities   | 69,418     |            |             |            |             |            |              |         | 69,418    |            |              |           |
| Short-term investments  |            |            |             |            |             |            |              |         |           |            |              |           |
| Total assets measured at fair value on a recurring basis      |            |            |             |            |             |            |              |         |           |            |              |           |
|   | \$ 960,044 | \$ 73,766  | \$ 44,768   | \$ (3,263) | \$ (37,934) | \$ 156,698 | \$ (108,368) | \$      | \$ 70,826 | \$ 1,661   | \$ 1,158,198 | \$ 72,266 |
| Annuity account balances(2)                                   | \$ 129,468 | \$         | \$ (3,686)  | \$         | \$          | \$ 201     | \$ 18,741    | \$      | \$        | \$ 114,614 | \$           |           |
| Total liabilities measured at fair value on a recurring basis |            |            |             |            |             |            |              |         |           |            |              |           |
|   | \$ 740,905 | \$ 304,493 | \$ (32,323) | \$         | \$          | \$ 201     | \$ 18,741    | \$      | \$        | \$ 450,195 | \$ 275,856   |           |

(1)Represents certain freestanding and embedded derivatives.

(2)Represents liabilities related to fixed indexed annuities.

For the six months ended June 30, 2013, \$70.8 million of securities were transferred into Level 3. This amount was transferred from Level 2. These transfers resulted from securities that were priced by independent pricing services or brokers in previous periods, using no significant unobservable inputs, but were priced internally using significant unobservable inputs where market observable inputs were no longer available as of June 30, 2013. All transfers are recognized as of the end of the period.

For the six months ended June 30, 2013, there were no transfers out of Level 3.

For the six months ended June 30, 2013, there were no transfers from Level 2 to Level 1.

For the six months ended June 30, 2013, there were no transfers out of Level 1.

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

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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 fixed 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 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 fixed indexed annuities.

*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:

|                                       | Fair Value Level | June 30, 2014    |                                       | As of December 31, 2013 |              |
|---------------------------------------|------------------|------------------|---------------------------------------|-------------------------|--------------|
|                                       |                  | Carrying Amounts | Fair Values<br>(Dollars In Thousands) | Carrying Amounts        | Fair Values  |
| <b>Assets:</b>                        |                  |                  |                                       |                         |              |
| Mortgage loans on real estate         | 3                | \$ 5,294,729     | \$ 5,821,043                          | \$ 5,493,492            | \$ 5,956,133 |
| Policy loans                          | 3                | 1,778,379        | 1,778,379                             | 1,815,744               | 1,815,744    |
| Fixed maturities, held-to-maturity(1) | 3                | 400,000          | 451,382                               | 365,000                 | 335,676      |
| <b>Liabilities:</b>                   |                  |                  |                                       |                         |              |
| Stable value product account balances | 3                | \$ 2,435,995     | \$ 2,456,141                          | \$ 2,559,552            | \$ 2,566,209 |
| Annuity account balances              | 3                | 11,071,468       | 10,665,435                            | 11,125,253              | 10,639,637   |
| <b>Debt:</b>                          |                  |                  |                                       |                         |              |
| Bank borrowings                       | 3                | \$ 345,000       | \$ 345,000                            | \$ 485,000              | \$ 485,000   |
| Senior Notes                          | 2                | 1,100,000        | 1,356,480                             | 1,100,000               | 1,294,675    |
| Subordinated debt securities          | 2                | 540,593          | 552,607                               | 540,593                 | 473,503      |
| Non-recourse funding obligations(2)   | 3                | 579,078          | 578,392                               | 562,448                 | 470,709      |

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

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(1) Security purchased from unconsolidated subsidiary, Red Mountain LLC.

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(2) Of this carrying amount, \$400.0 million, fair value of \$427.1 million, as of June 30, 2014, and \$365.0 million, fair value of \$321.5 million, as of December 31, 2013, relates to non-recourse funding obligations issued by Golden Gate V.

### **Fair Value Measurements**

#### *Mortgage loans on real estate*

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



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***Policy loans***

The Company believes the fair value of policy loans approximates book value. Policy loans are funds provided to policy holders in return for a claim on the policy. The funds provided are limited to the cash surrender value of the underlying policy. The nature of policy loans is to have a negligible default risk as the loans are fully collateralized by the value of the policy. Policy loans do not have a stated maturity and the balances and accrued interest are repaid either by the policyholder or with proceeds from the policy. Due to the collateralized nature of policy loans and unpredictable timing of repayments, the Company believes the fair value of policy loans approximates carrying value.

***Fixed maturities, held-to-maturity***

The Company estimates the fair value of its fixed maturity, held-to-maturity securities using internal discounted cash flow models. The discount rates used in the model were based on a current market yield for similar financial instruments.

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

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

***Debt***

***Bank borrowings***

The Company believes the carrying value of its bank borrowings approximates fair value as the borrowings pay a floating interest rate plus a spread based on the rating of the Company's senior debt which the Company believes approximates a market interest rate.

***Non-recourse funding obligations***

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

17. **DERIVATIVE FINANCIAL INSTRUMENTS**

**Types of Derivative Instruments and Derivative Strategies**

The Company utilizes a risk management strategy that incorporates the use of derivative financial instruments to reduce exposure to certain risks, including but not limited to, interest rate risk, inflation risk, currency exchange risk, volatility risk, and equity market risk. These strategies are developed through the Company's analysis of data from financial simulation models and other internal and industry sources, and are then incorporated into the Company's risk management program.

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

*Derivatives Related to Interest Rate Risk Management*

Derivative instruments that are used as part of the Company's interest rate risk management strategy include interest rate swaps, interest rate futures, interest rate caps, and interest rate swaptions. The Company's inflation risk

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management strategy involves the use of swaps that requires the Company to pay a fixed rate and receive a floating rate that is based on changes in the Consumer Price Index ( CPI ).

*Derivatives Related to Risk Mitigation of Certain Annuity Contracts*

The Company may use the following types of derivative contracts to mitigate its exposure to certain guaranteed benefits related to variable annuity contracts and fixed indexed annuities:

- Foreign Currency Futures
- Variance Swaps
- Interest Rate Futures
- Equity Options
- Equity Futures
- Credit Derivatives
- Interest Rate Swaps
- Interest Rate Swaptions
- Volatility Futures
- Volatility Options
- Total Return Swaps

**Accounting for Derivative Instruments**

The Company records its derivative financial instruments in the consolidated condensed balance sheet in other long-term investments and other liabilities in accordance with GAAP, which requires that all derivative instruments be recognized in the balance sheet at fair value. The change in the fair value of derivative financial instruments is reported either in the statement of income or in other comprehensive income (loss), depending upon whether it qualified for and also has been properly identified as being part of a hedging relationship, and also on the type of hedging relationship that exists.

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For a derivative financial instrument to be accounted for as an accounting hedge, it must be identified and documented as such on the date of designation. For cash flow hedges, the effective portion of their realized gain or loss is reported as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged item impacts earnings. Any remaining gain or loss, the ineffective portion, is recognized in current earnings. For fair value hedge derivatives, their gain or loss, as well as the offsetting loss or gain attributable to the hedged risk of the hedged item, is recognized in current earnings. Effectiveness of the Company's hedge relationships is assessed on a quarterly basis.

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

### **Derivative Instruments Designated and Qualifying as Hedging Instruments**

#### **Cash-Flow Hedges**

- In connection with the issuance of inflation-adjusted funding agreements, the Company has entered into swaps to convert the floating CPI-linked interest rate on these agreements to a fixed rate. The Company pays a fixed rate on the swap and receives a floating rate primarily determined by the period's change in the CPI. The amounts that are received on the swaps are equal to the amounts that are paid on the agreements.

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

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

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**Derivatives Related to Variable Annuity Contracts**

- The Company uses equity, interest rate, currency, and volatility futures to mitigate the risk related to certain guaranteed minimum benefits, including GMWB, within its VA products. In general, the cost of such benefits varies with the level of equity and interest rate markets, foreign currency levels, and overall volatility. No volatility future positions were held as of June 30, 2014.
- The Company uses equity options, variance swaps, and volatility options to mitigate the risk related to certain guaranteed minimum benefits, including GMWB, within its VA products. In general, the cost of such benefits varies with the level of equity markets and overall volatility. No volatility option positions were held as of June 30, 2014.
- The Company uses interest rate swaps and interest rate swaptions to mitigate the risk related to certain guaranteed minimum benefits, including GMWB, within its VA products.
- The Company markets certain VA products with a GMWB rider. The GMWB component is considered an embedded derivative, not considered to be clearly and closely related to the host contract.

**Derivatives Related to Fixed Annuity Contracts**

- The Company uses equity and volatility futures to mitigate the risk within its fixed indexed annuity products. In general, the cost of such benefits varies with the level of equity and overall volatility.
- The Company used equity options to mitigate the risk within its fixed indexed annuity products. In general, the cost of such benefits varies with the level of equity markets.
- The Company markets certain fixed indexed annuity products. The FIA component is considered an embedded derivative, not considered to be clearly and closely related to the host contract.

**Other Derivatives**

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- The Company uses certain interest rate swaps to mitigate the price volatility of fixed maturities. None of these positions were held as of June 30, 2014.
- The Company purchased interest rate caps to mitigate its risk with respect to the Company's LIBOR exposure and the potential impact of European financial market distress. None of these positions were held as of June 30, 2014.
- The Company uses various swaps and other types of derivatives to manage risk related to other exposures.
- The Company markets certain IUL products. The IUL component is considered an embedded derivative, not considered to be clearly and closely related to the host contract.
- The Company is involved in various modified coinsurance and funds withheld arrangements which contain embedded derivatives. Changes in their fair value are recorded in current period earnings. The investment portfolios that support the related modified coinsurance reserves and funds withheld arrangements had fair value changes which substantially offset the gains or losses on these embedded derivatives.

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The following table sets forth realized investments gains and losses for the periods shown:

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

|   | For The<br>Three Months Ended<br>June 30, |            | For The<br>Six Months Ended<br>June 30, |             |
|---|---|------------|---|-------------|
|   | 2014                                      | 2013       | 2014                                    | 2013        |
|   | (Dollars In Thousands)                    |            |   |             |
| Derivatives related to variable annuity contracts:      |   |            |   |             |
| Interest rate futures - VA                              | \$ 6,548                                  | \$ (7,654) | \$ 10,798                               | \$ (24,138) |
| Equity futures - VA                                     | (7,259)                                   | (4,036)    | (9,910)                                 | (27,261)    |
| Currency futures - VA                                   | (2,887)                                   | (112)      | (4,165)                                 | 7,971       |
| Variance swaps - VA                                     | (823)                                     | 2,214      | (2,673)                                 | (8,219)     |
| Equity options - VA                                     | (20,949)                                  | (8,131)    | (33,290)                                | (36,537)    |
| Interest rate swaptions - VA                            | (4,998)                                   | 1,639      | (14,401)                                | (2,463)     |
| Interest rate swaps - VA                                | 45,169                                    | (89,722)   | 102,537                                 | (106,278)   |
| Embedded derivative - GMWB                              | (47,389)                                  | 103,315    | (129,676)                               | 183,690     |
| Total derivatives related to variable annuity contracts | (32,588)                                  | (2,487)    | (80,780)                                | (13,235)    |
| Derivatives related to FIA contracts:                   |   |            |   |             |
| Embedded derivative - FIA                               | (8,307)                                   | (41)       | (6,574)                                 | (41)        |
| Equity futures - FIA                                    | 605                                       |            | 950                                     |             |
| Volatility futures - FIA                                | 8   |            | 8                                       |             |
| Equity options - FIA                                    | 2,984                                     | (19)       | 3,978                                   | (19)        |
| Total derivatives related to FIA contracts              | (4,710)                                   | (60)       | (1,638)                                 | (60)        |
| Embedded derivative - IUL                               | (285)                                     |            | (285)                                   |             |
| Embedded derivative - Modco reinsurance treaties        | (52,202)                                  | 144,998    | (112,371)                               | 161,773     |
| Interest rate swaps                                     |   | 1,909      |   | 2,912       |
| Other derivatives                                       | (141)                                     | (479)      | (202)                                   | (124)       |
| Total realized gains (losses) - derivatives             | \$ (89,926)                               | \$ 143,881 | \$ (195,276)                            | \$ 151,266  |

The following table sets forth realized investments gains and losses for Modco trading portfolio that is included in realized investment gains (losses) all other investments.

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

|                            |           |              |            |              |
|----------------------------|-----------|--------------|------------|--------------|
| Modco trading portfolio(1) | \$ 60,989 | \$ (126,694) | \$ 127,292 | \$ (142,022) |
|----------------------------|-----------|--------------|------------|--------------|

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



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The following table presents the components of the gain or loss on derivatives that qualify as a cash flow hedging relationship.

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

|   | Amount of Gains (Losses)<br>Deferred in<br>Accumulated Other<br>Comprehensive Income<br>(Loss) on Derivatives<br>(Effective Portion) | Amount and Location of<br>Gains (Losses)<br>Reclassified from<br>Accumulated Other<br>Comprehensive Income<br>(Loss) into Income (Loss)<br>(Effective Portion)<br>Benefits and settlement<br>expenses<br>(Dollars In Thousands) | Amount and Location of<br>(Losses) Recognized in<br>Income (Loss) on<br>Derivatives<br>(Ineffective Portion)<br>Realized investment<br>gains (losses) |
|---|--|---|---|
| <b>For The Three Months Ended June 30, 2014</b> |  |   |   |
| Inflation                                       | \$ (929)   | \$ (614)  | \$ (165)  |
| Total   | \$ (929)   | \$ (614)  | \$ (165)  |
| <b>For The Six Months Ended June 30, 2014</b>   |  |   |   |
| Inflation                                       | \$ (26)  | \$ (1,284)  | \$ (126)  |
| Total   | \$ (26)  | \$ (1,284)  | \$ (126)  |

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

|   | Amount of Gains (Losses)<br>Deferred in<br>Accumulated Other<br>Comprehensive Income<br>(Loss) on Derivatives<br>(Effective Portion) | Amount and Location of<br>Gains (Losses)<br>Reclassified from<br>Accumulated Other<br>Comprehensive Income<br>(Loss) into Income (Loss)<br>(Effective Portion)<br>Benefits and settlement<br>expenses<br>(Dollars In Thousands) | Amount and Location of<br>(Losses) Recognized in<br>Income (Loss) on<br>Derivatives<br>(Ineffective Portion)<br>Realized investment<br>gains (losses) |
|---|--|---|---|
| <b>For The Three Months Ended June 30, 2013</b> |  |   |   |
| Inflation                                       | \$ (4,589)   | \$ (580)  | \$ (558)  |
| Total   | \$ (4,589)   | \$ (580)  | \$ (558)  |
| <b>For The Six Months Ended June 30, 2013</b>   |  |   |   |
| Inflation                                       | \$ (180)   | \$ (1,077)  | \$ (190)  |
| Total   | \$ (180)   | \$ (1,077)  | \$ (190)  |

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

|  | As of June 30, 2014 |            | As of December 31, 2013 |            |
|--|---------------------|------------|-------------------------|------------|
|  | Notional Amount     | Fair Value | Notional Amount         | Fair Value |
| (Dollars In Thousands)                             |                     |            |                         |            |
| <b>Other long-term investments</b>                 |                     |            |                         |            |
| Cash flow hedges:                                  |                     |            |                         |            |
| Inflation  | \$                  | \$         | \$                      | \$         |
| Derivatives not designated as hedging instruments: |                     |            |                         |            |
| Interest rate swaps                                | 295,000             | 3,681      | 200,000                 | 1,961      |
| Embedded derivative - Modco reinsurance treaties   | 30,105              | 1,226      | 80,376                  | 1,517      |
| Embedded derivative - GMWB                         | 5,161,813           | 122,075    | 6,113,017               | 194,616    |
| Interest rate futures                              | 283,629             | 1,510      |                         |            |
| Equity futures                                     | 46,915              | 379        | 3,387                   | 111        |
| Currency futures                                   |                     |            | 14,338                  | 321        |
| Equity options                                     | 2,051,427           | 120,586    | 1,376,205               | 78,277     |
| Interest rate swaptions                            | 625,000             | 15,890     | 625,000                 | 30,291     |
| Other  | 592                 | 420        | 425                     | 473        |
|  | \$ 8,494,481        | \$ 265,767 | \$ 8,412,748            | \$ 307,567 |
| <b>Other liabilities</b>                           |                     |            |                         |            |
| Cash flow hedges:                                  |                     |            |                         |            |
| Inflation  | \$ 182,965          | \$ 624     | \$ 182,965              | \$ 1,865   |
| Derivatives not designated as hedging instruments: |                     |            |                         |            |
| Interest rate swaps                                | 1,180,000           | 59,968     | 1,230,000               | 153,322    |
| Variance swaps                                     | 1,100               | 3,782      | 1,500                   | 1,744      |
| Embedded derivative - Modco reinsurance treaties   | 2,591,360           | 318,999    | 2,578,590               | 206,918    |
| Embedded derivative - GMWB                         | 4,418,599           | 95,523     | 2,494,142               | 38,388     |
| Embedded derivative - FIA                          | 527,698             | 69,615     | 244,424                 | 25,324     |
| Embedded derivative - IUL                          | 1,057               | 610        |                         |            |
| Interest rate futures                              | 71,714              | 37         | 322,902                 | 5,221      |
| Equity futures                                     | 102,891             | 1,443      | 164,595                 | 6,595      |
| Currency futures                                   | 138,916             | 2,364      | 118,008                 | 840        |
| Equity options                                     | 475,155             | 32,726     | 257,065                 | 17,558     |
| Other  | 358                 | 38         | 230                     | 27         |
|  | \$ 9,691,813        | \$ 585,729 | \$ 7,594,421            | \$ 457,802 |

Based on the expected cash flows of the underlying hedged items, the Company expects to reclassify \$0.5 million out of accumulated other comprehensive income (loss) into earnings during the next twelve months.

**18. OFFSETTING OF ASSETS AND LIABILITIES**

Certain of the Company's derivative instruments are subject to enforceable master netting arrangements that provide for the net settlement of all derivative contracts between the Company and a counterparty in the event of default or upon the occurrence of certain termination events. Collateral support agreements associated with each master netting arrangement provide that the Company will receive or pledge financial collateral in the event either minimum thresholds, or in certain cases ratings levels, have been reached. Additionally, certain of the Company's repurchase agreements provide for net settlement on termination of the agreement. Refer to Note 9, *Debt and Other Obligations* for details of the

Company's repurchase agreement programs.

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The tables below present the derivative instruments by assets and liabilities for the Company as of June 30, 2014:

|  | Gross<br>Amounts of<br>Recognized<br>Assets | Gross<br>Amounts<br>Offset in the<br>Statement of<br>Financial<br>Position | Net Amounts<br>of Assets<br>Presented in<br>the<br>Statement of<br>Financial<br>Position<br>(Dollars In Thousands) | Gross Amounts Not Offset<br>in the Statement of<br>Financial Position<br>Financial<br>Instruments | Cash<br>Collateral<br>Received | Net Amount        |
|--|---|--|--|---|--------------------------------|-------------------|
| <b>Offsetting of Derivative Assets</b>   |   |  |  |   |                                |                   |
| Derivatives:   |   |  |  |   |                                |                   |
| Free-Standing derivatives  | \$ 142,090                                  | \$   | \$ 142,090   | \$ 54,682   | \$ 23,039                      | \$ 64,369         |
| Embedded derivative -<br>Modco reinsurance treaties  | 1,226                                       |  | 1,226  |   |                                | 1,226             |
| Embedded derivative -<br>GMWB  | 122,075                                     |  | 122,075  |   |                                | 122,075           |
| Total derivatives, subject to a<br>master netting arrangement or<br>similar arrangement        | 265,391                                     |  | 265,391  | 54,682  | 23,039                         | 187,670           |
| Total derivatives, not subject<br>to a master netting<br>arrangement or similar<br>arrangement | 376   |  | 376  |   |                                | 376               |
| Total derivatives  | 265,767                                     |  | 265,767  | 54,682  | 23,039                         | 188,046           |
| <b>Total Assets</b>  | <b>\$ 265,767</b>                           | <b>\$</b>  | <b>\$ 265,767</b>  | <b>\$ 54,682</b>  | <b>\$ 23,039</b>               | <b>\$ 188,046</b> |

|  | Gross<br>Amounts of<br>Recognized<br>Liabilities | Gross<br>Amounts<br>Offset in the<br>Statement of<br>Financial<br>Position | Net Amounts<br>of Liabilities<br>Presented in<br>the<br>Statement of<br>Financial<br>Position<br>(Dollars In Thousands) | Gross Amounts Not Offset<br>in the Statement of<br>Financial Position<br>Financial<br>Instruments | Cash<br>Collateral<br>Paid | Net Amount |
|--|--|--|---|---|----------------------------|------------|
| <b>Offsetting of Derivative Liabilities</b>  |  |  |   |   |                            |            |
| Derivatives:   |  |  |   |   |                            |            |
| Free-Standing derivatives  | \$ 100,982                                       | \$   | \$ 100,982  | \$ 54,682   | \$ 46,113                  | \$ 187     |
| Embedded derivative - Modco<br>reinsurance treaties  | 318,999  |  | 318,999   |   |                            | 318,999    |
| Embedded derivative -<br>GMWB  | 95,523   |  | 95,523  |   |                            | 95,523     |
| Embedded derivative - FIA  | 69,615   |  | 69,615  |   |                            | 69,615     |
| Embedded derivative - IUL  | 610  |  | 610   |   |                            | 610        |
| Total derivatives, subject to a<br>master netting arrangement or<br>similar arrangement        | 585,729  |  | 585,729   | 54,682  | 46,113                     | 484,934    |
| Total derivatives, not subject<br>to a master netting<br>arrangement or similar<br>arrangement |  |  |   |   |                            |            |
| Total derivatives  | 585,729  |  | 585,729   | 54,682  | 46,113                     | 484,934    |

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|                          |              |    |              |    |        |    |        |    |         |
|--------------------------|--------------|----|--------------|----|--------|----|--------|----|---------|
| Repurchase agreements(1) | 420,490      |    | 420,490      |    |        |    |        |    | 420,490 |
| <b>Total Liabilities</b> | \$ 1,006,219 | \$ | \$ 1,006,219 | \$ | 54,682 | \$ | 46,113 | \$ | 905,424 |

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(1) Borrowings under repurchase agreements are for a term less than 90 days.

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The tables below present the derivative instruments by assets and liabilities for the Company as of December 31, 2013:

|   | Gross<br>Amounts of<br>Recognized<br>Assets | Gross<br>Amounts<br>Offset in the<br>Statement of<br>Financial<br>Position | Net Amounts<br>of Assets<br>Presented in<br>the<br>Statement of<br>Financial<br>Position<br>(Dollars In Thousands) | Gross Amounts Not Offset<br>in the Statement of<br>Financial Position<br><br>Financial<br>Instruments | Cash<br>Collateral<br>Received | Net Amount        |
|---|---|--|--|---|--------------------------------|-------------------|
| <b>Offsetting of Derivative Assets</b>  |   |  |  |   |                                |                   |
| Derivatives:  |   |  |  |   |                                |                   |
| Free-Standing derivatives   | \$ 110,983                                  | \$   | \$ 110,983   | \$ 52,487   | \$ 10,700                      | \$ 47,796         |
| Embedded derivative - Modco reinsurance treaties                                      | 1,517                                       |  | 1,517  |   |                                | 1,517             |
| Embedded derivative - GMWB  | 194,616                                     |  | 194,616  |   |                                | 194,616           |
| Total derivatives, subject to a master netting arrangement or similar arrangement     | 307,116                                     |  | 307,116  | 52,487  | 10,700                         | 243,929           |
| Total derivatives, not subject to a master netting arrangement or similar arrangement | 451   |  | 451  |   |                                | 451               |
| Total derivatives   | 307,567                                     |  | 307,567  | 52,487  | 10,700                         | 244,380           |
| <b>Total Assets</b>   | <b>\$ 307,567</b>                           | <b>\$</b>  | <b>\$ 307,567</b>  | <b>\$ 52,487</b>  | <b>\$ 10,700</b>               | <b>\$ 244,380</b> |

|   | Gross<br>Amounts of<br>Recognized<br>Liabilities | Gross<br>Amounts<br>Offset in the<br>Statement of<br>Financial<br>Position | Net Amounts<br>of Liabilities<br>Presented in<br>the<br>Statement of<br>Financial<br>Position<br>(Dollars In Thousands) | Gross Amounts Not Offset<br>in the Statement of<br>Financial Position<br><br>Financial<br>Instruments | Cash<br>Collateral<br>Paid | Net Amount        |
|---|--|--|---|---|----------------------------|-------------------|
| <b>Offsetting of Derivative Liabilities</b>   |  |  |   |   |                            |                   |
| Derivatives:  |  |  |   |   |                            |                   |
| Free-Standing derivatives   | \$ 187,172                                       | \$   | \$ 187,172  | \$ 52,487   | \$ 98,359                  | \$ 36,326         |
| Embedded derivative - Modco reinsurance treaties                                      | 206,918  |  | 206,918   |   |                            | 206,918           |
| Embedded derivative - GMWB  | 38,388   |  | 38,388  |   |                            | 38,388            |
| Embedded derivative - FIA   | 25,324   |  | 25,324  |   |                            | 25,324            |
| Total derivatives, subject to a master netting arrangement or similar arrangement     | 457,802  |  | 457,802   | 52,487  | 98,359                     | 306,956           |
| Total derivatives, not subject to a master netting arrangement or similar arrangement |  |  |   |   |                            |                   |
| Total derivatives   | 457,802  |  | 457,802   | 52,487  | 98,359                     | 306,956           |
| Repurchase agreements(1)  | 350,000  |  | 350,000   |   |                            | 350,000           |
| <b>Total Liabilities</b>  | <b>\$ 807,802</b>                                | <b>\$</b>  | <b>\$ 807,802</b>   | <b>\$ 52,487</b>  | <b>\$ 98,359</b>           | <b>\$ 656,956</b> |

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(1) Borrowings under repurchase agreements are for a term less than 90 days.

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**19. OPERATING SEGMENTS**

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

- The Life Marketing segment markets fixed universal life ( UL ), variable universal life ( VUL ), bank-owned life insurance ( BOLI ), and level premium term insurance ( traditional ) products on a national basis primarily through networks of independent insurance agents and brokers, broker-dealers, financial institutions, and independent marketing organizations.
- The Acquisitions segment focuses on acquiring, converting, and servicing policies acquired from other companies. The segment's primary focus is on life insurance policies and annuity products that were sold to individuals. The level of the segment's acquisition activity is predicated upon many factors, including available capital, operating capacity, potential return on capital, and market dynamics. Policies acquired through the Acquisitions segment are typically blocks of business where no new policies are being marketed. Therefore earnings and account values are expected to decline as the result of lapses, deaths, and other terminations of coverage unless new acquisitions are made.
- The Annuities segment markets fixed and variable annuity products. These products are primarily sold through broker-dealers, financial institutions, and independent agents and brokers.
- The Stable Value Products segment sells fixed and floating rate funding agreements directly to the trustees of municipal bond proceeds, money market funds, bank trust departments, and other institutional investors. The segment also issues funding agreements to the FHLB, and markets guaranteed investment contracts ( GICs ) to 401(k) and other qualified retirement savings plans. Additionally, the Company has contracts outstanding pursuant to a funding agreement-backed notes program registered with the United States Securities and Exchange Commission (the SEC ) which offered notes to both institutional and retail investors.
- The Asset Protection segment markets extended service contracts and credit life and disability insurance to protect consumers investments in automobiles, watercraft, and recreational vehicles. In addition, the segment markets a guaranteed asset protection ( GAP ) product. GAP coverage covers the difference between the loan pay-off amount and an asset's actual cash value in the case of a total loss.
- The Corporate and Other segment primarily consists of net investment income not assigned to the segments above (including the impact of carrying liquidity) and expenses not attributable to the segments above (including interest on certain corporate debt). This segment includes earnings from several non-strategic or runoff lines of business, various investment-related transactions, the operations of several small subsidiaries, and the repurchase of non-recourse funding obligations.



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The Company uses the same accounting policies and procedures to measure segment operating income (loss) and assets as it uses to measure consolidated net income and assets. Segment operating income (loss) is income before income tax, excluding realized gains and losses on investments and derivatives net of the amortization related to deferred acquisition costs ( DAC ), value of business acquired ( VOBA ), and benefits and settlement expenses. Operating earnings exclude changes in the GMWB embedded derivatives (excluding the portion attributed to economic cost), realized and unrealized gains (losses) on derivatives used to hedge the VA product, actual GMWB incurred claims and the related amortization of DAC attributed to each of these items.

Segment operating income (loss) represents the basis on which the performance of the Company's business is internally assessed by management. Premiums and policy fees, other income, benefits and settlement expenses, and amortization of DAC/VOBA are attributed directly to each operating segment. Net investment income is allocated based on directly related assets required for transacting the business of that segment. Realized investment gains (losses) and other operating expenses are allocated to the segments in a manner that most appropriately reflects the operations of

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that segment. Investments and other assets are allocated based on statutory policy liabilities net of associated statutory policy assets, while DAC/VOBA and goodwill are shown in the segments to which they are attributable.

There were no significant intersegment transactions during the three or six months ended June 30, 2014 and 2013.

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

|  |    |           |    |           |    |           |    |           |
|--|----|-----------|----|-----------|----|-----------|----|-----------|
|  |    |           |    |           |    |           |    |           |
| <b>Revenues</b>  |    |           |    |           |    |           |    |           |
| Life Marketing   | \$ | 407,032   | \$ | 347,021   | \$ | 791,798   | \$ | 714,647   |
| Acquisitions   |    | 438,244   |    | 261,693   |    | 865,192   |    | 512,180   |
| Annuities  |    | 155,417   |    | 186,025   |    | 300,074   |    | 350,954   |
| Stable Value Products  |    | 27,109    |    | 34,468    |    | 54,928    |    | 66,388    |
| Asset Protection   |    | 70,870    |    | 71,813    |    | 137,253   |    | 139,384   |
| Corporate and Other  |    | 56,671    |    | 55,336    |    | 96,656    |    | 105,617   |
| Total revenues   | \$ | 1,155,343 | \$ | 956,356   | \$ | 2,245,901 | \$ | 1,889,170 |
| <b>Segment Operating Income (Loss)</b>                                   |    |           |    |           |    |           |    |           |
| Life Marketing   | \$ | 26,349    | \$ | 24,673    | \$ | 49,834    | \$ | 48,380    |
| Acquisitions   |    | 64,882    |    | 29,435    |    | 125,878   |    | 63,812    |
| Annuities  |    | 55,258    |    | 36,382    |    | 106,901   |    | 79,780    |
| Stable Value Products  |    | 17,287    |    | 22,464    |    | 34,684    |    | 40,308    |
| Asset Protection   |    | 8,534     |    | 7,384     |    | 14,903    |    | 13,465    |
| Corporate and Other  |    | (12,555)  |    | (2,483)   |    | (27,410)  |    | (20,815)  |
| Total segment operating income   |    | 159,755   |    | 117,855   |    | 304,790   |    | 224,930   |
| Realized investment (losses) gains - investments(1)                      |    | 74,920    |    | (119,311) |    | 143,453   |    | (129,067) |
| Realized investment (losses) gains - derivatives                         |    | (72,465)  |    | 158,469   |    | (160,828) |    | 178,777   |
| Income tax expense   |    | (54,233)  |    | (53,814)  |    | (95,799)  |    | (93,150)  |
| Net income   | \$ | 107,977   | \$ | 103,199   | \$ | 191,616   | \$ | 181,490   |
| Investment gains (losses)(2)   | \$ | 78,688    | \$ | (113,978) | \$ | 149,211   | \$ | (122,707) |
| Less: amortization related to DAC/VOBA and benefits settlements expenses |    | 3,768     |    | 5,333     |    | 5,758     |    | 6,360     |
| Realized investment gains (losses) - investments                         | \$ | 74,920    | \$ | (119,311) | \$ | 143,453   | \$ | (129,067) |
| Derivative gains (losses)(3)   | \$ | (89,926)  | \$ | 143,881   | \$ | (195,276) | \$ | 151,266   |
| Less: VA GMWB economic cost  |    | (17,461)  |    | (14,588)  |    | (34,448)  |    | (27,511)  |
| Realized investment gains (losses) - derivatives                         | \$ | (72,465)  | \$ | 158,469   | \$ | (160,828) | \$ | 178,777   |

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(1) Includes credit related other-than-temporary impairments of \$1.5 million and \$3.1 million for the three and six months ended June 30, 2014, respectively, as compared to \$4.0 million and \$8.6 million for the three and six months ended June 30, 2013, respectively.

(2) Includes realized investment gains (losses) before related amortization.

(3) Includes realized gains (losses) on derivatives before the VA GMWB economic cost.

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| <b>Operating Segment Assets<br/>As of June 30, 2014<br/>(Dollars In Thousands)</b> |                           |                     |                  |                                  |
|--|---------------------------|---------------------|------------------|----------------------------------|
|  | <b>Life<br/>Marketing</b> | <b>Acquisitions</b> | <b>Annuities</b> | <b>Stable Value<br/>Products</b> |
| Investments and other assets   | \$ 13,575,287             | \$ 20,179,754       | \$ 20,713,485    | \$ 2,435,193                     |
| Deferred policy acquisition costs and value of business acquired                   | 2,000,329                 | 605,799             | 623,461          | 802                              |
| Goodwill   | 10,192                    | 30,968              |                  |                                  |
| Total assets   | \$ 15,585,808             | \$ 20,816,521       | \$ 21,336,946    | \$ 2,435,995                     |

|  | <b>Asset<br/>Protection</b> | <b>Corporate<br/>and Other</b> | <b>Adjustments</b> | <b>Total<br/>Consolidated</b> |
|--|-----------------------------|--------------------------------|--------------------|-------------------------------|
| Investments and other assets                                     | \$ 894,935                  | \$ 9,966,477                   | \$ 15,644          | \$ 67,780,775                 |
| Deferred policy acquisition costs and value of business acquired | 42,397                      | 487                            |                    | 3,273,275                     |
| Goodwill   | 62,671                      | 83                             |                    | 103,914                       |
| Total assets   | \$ 1,000,003                | \$ 9,967,047                   | \$ 15,644          | \$ 71,157,964                 |

| <b>Operating Segment Assets<br/>As of December 31, 2013<br/>(Dollars In Thousands)</b> |                           |                     |                  |                                  |
|--|---------------------------|---------------------|------------------|----------------------------------|
|  | <b>Life<br/>Marketing</b> | <b>Acquisitions</b> | <b>Annuities</b> | <b>Stable Value<br/>Products</b> |
| Investments and other assets   | \$ 13,135,914             | \$ 20,186,839       | \$ 19,974,246    | \$ 2,558,551                     |
| Deferred policy acquisition costs and value of business acquired                       | 2,071,470                 | 799,255             | 647,485          | 1,001                            |
| Goodwill   | 10,192                    | 32,517              |                  |                                  |
| Total assets   | \$ 15,217,576             | \$ 21,018,611       | \$ 20,621,731    | \$ 2,559,552                     |

|  | <b>Asset<br/>Protection</b> | <b>Corporate<br/>and Other</b> | <b>Adjustments</b> | <b>Total<br/>Consolidated</b> |
|--|-----------------------------|--------------------------------|--------------------|-------------------------------|
| Investments and other assets                                     | \$ 852,273                  | \$ 8,355,618                   | \$ 16,762          | \$ 65,080,203                 |
| Deferred policy acquisition costs and value of business acquired | 50,358                      | 646                            |                    | 3,570,215                     |
| Goodwill   | 62,671                      | 83                             |                    | 105,463                       |
| Total assets   | \$ 965,302                  | \$ 8,356,347                   | \$ 16,762          | \$ 68,755,881                 |

**20. SUBSEQUENT EVENTS**

The Company has evaluated the effects of events subsequent to June 30, 2014, and through the date we filed our consolidated condensed financial statements with the United States Securities and Exchange Commission. All accounting and disclosure requirements related to subsequent events are included in our consolidated condensed financial statements.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) should be read in conjunction with our consolidated condensed financial statements included under Part I, Item 1, *Financial Statements (Unaudited)*, of this Quarterly Report on Form 10-Q and our audited consolidated financial statements for the year ended December 31, 2013, included in our Annual Report on Form 10-K.

For a more complete understanding of our business and current period results, please read the following MD&A in conjunction with our latest Annual Report on Form 10-K and other filings with the United States Securities and Exchange Commission (the SEC ).

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

**FORWARD-LOOKING STATEMENTS CAUTIONARY LANGUAGE**

This report reviews our financial condition and results of operations including our liquidity and capital resources. Historical information is presented and discussed, and where appropriate, factors that may affect future financial performance are also identified and discussed. Certain statements made in this report include forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include any statement that may predict, forecast, indicate, or imply future results, performance, or achievements instead of historical facts and may contain words like believe, expect, estimate, project, budget, forecast, anticipate, plan, will, other words, phrases, or expressions with similar meaning. Forward-looking statements involve risks and uncertainties, which may cause actual results to differ materially from the results contained in the forward-looking statements, and we cannot give assurances that such statements will prove to be correct. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future developments or otherwise. For more information about the risks, uncertainties, and other factors that could affect our future results, please refer to Part I, Item 2, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, Risks and Uncertainties and Part II, Item 1A, *Risk Factors and Cautionary Factors that may Affect Future Results*, of this report, as well as Part I, Item 1A, *Risk Factors and Cautionary Factors that may Affect Future Results*, of our Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

**OVERVIEW**

*Our business*

We are a holding company headquartered in Birmingham, Alabama, with subsidiaries that provide financial services through the production, distribution, and administration of insurance and investment products. Founded in 1907, Protective Life Insurance Company ( PLICO ) is our largest operating subsidiary. Unless the context otherwise requires, the Company, we, us, or our refers to the consolidated group of Protective Life Corporation and our subsidiaries.

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We have several operating segments, each having a strategic focus. An operating segment is distinguished by products, channels of distribution, and/or other strategic distinctions. We periodically evaluate our operating segments as prescribed in the Accounting Standards Codification ( ASC ) Segment Reporting Topic, and make adjustments to our segment reporting as needed.

Our operating segments are Life Marketing, Acquisitions, Annuities, Stable Value Products, Asset Protection, and Corporate and Other.

- **Life Marketing** - We market fixed universal life ( UL ), variable universal life ( VUL ), bank-owned life insurance ( BOLI ), and level premium term insurance ( traditional ) products on a national basis

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primarily through networks of independent insurance agents and brokers, broker-dealers, financial institutions, and independent marketing organizations.

- **Acquisitions** - We focus on acquiring, converting, and servicing policies from other companies. The segment's primary focus is on life insurance policies and annuity products that were sold to individuals. The level of the segment's acquisition activity is predicated upon many factors, including available capital, operating capacity, potential return on capital, and market dynamics. Policies acquired through the Acquisitions segment are typically blocks of business where no new policies are being marketed. Therefore earnings and account values are expected to decline as the result of lapses, deaths, and other terminations of coverage unless new acquisitions are made.
- **Annuities** - We market fixed and variable annuity ( VA ) products. These products are primarily sold through broker-dealers, financial institutions, and independent agents and brokers.
- **Stable Value Products** - We sell fixed and floating rate funding agreements directly to the trustees of municipal bond proceeds, money market funds, bank trust departments, and other institutional investors. The segment also issues funding agreements to the Federal Home Loan Bank ( FHLB ), and markets guaranteed investment contracts ( GICs ) to 401(k) and other qualified retirement savings plans. Additionally, we have contracts outstanding pursuant to a funding agreement-backed notes program registered with the SEC which offered notes to both institutional and retail investors.
- **Asset Protection** - We market extended service contracts and credit life and disability insurance to protect consumers' investments in automobiles, watercraft, and recreational vehicles. In addition, the segment markets a guaranteed asset protection ( GAP ) product. GAP coverage covers the difference between the loan pay-off amount and an asset's actual cash value in the case of a total loss.
- **Corporate and Other** - This segment primarily consists of net investment income not assigned to the segments above (including the impact of carrying liquidity) and expenses not attributable to the segments above (including interest on certain corporate debt). This segment includes earnings from several non-strategic or runoff lines of business, various investment-related transactions, the operations of several small subsidiaries, and the repurchase of non-recourse funding obligations.

**EXECUTIVE SUMMARY**

Net income for the first six months of 2014 was \$191.6 million or \$2.36 per average diluted share. After-tax operating income for the first six months of 2014 was \$202.9 million or \$2.50 per average diluted share.

We reported strong financial results for the first six months of 2014. The MONY acquisition integration is on track and has made a significant contribution to the Acquisitions segment earnings during the first six months of this year. With strong financial results for the first half of 2014, we remain confident in our ability to execute on our plans for the remainder of the year.

Significant financial information related to each of our segments is included in Results of Operations .

## RECENT DEVELOPMENTS PROPOSED DAI-ICHI MERGER

As described in Note 5, *Proposed Dai-ichi Merger*, to the consolidated condensed financial statements, on June 3, 2014, we entered into an Agreement and Plan of Merger (the Merger Agreement ) with The Dai-ichi Life Insurance Company, Limited, a *kabushiki kaisha* organized under the laws of Japan ( Dai-ichi ) and DL Investment (Delaware), Inc., a Delaware corporation and wholly owned subsidiary of Dai-ichi, which provides for the merger of DL Investment (Delaware), Inc. with and into the Company (the Merger ), with the Company surviving the Merger as a wholly owned subsidiary of Dai-ichi. If the proposed Merger is completed, at the effective time of the Merger (the Effective Time ), each share of our common stock, par value \$0.50 per share, issued and outstanding immediately prior to the Effective Time, other than certain excluded shares, will be converted into the right to receive \$70 in cash, without interest (the Per Share Merger Consideration ). Shares of common stock held by Dai-ichi or the Company or their respective direct or indirect wholly-owned subsidiaries will not be entitled to receive the Merger Consideration. Stock appreciation rights, restricted stock units and performance shares issued under various benefit plans will be paid out as described in Note 5, *Proposed Dai-ichi Merger*, to the consolidated condensed financial statements included in this report, under the heading Treatment of Benefit Plans .

Completion of the Merger is subject to various closing conditions, including, but not limited to, (1) adoption of the Merger Agreement by the affirmative vote of the holders of at least a majority of all outstanding shares of common



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stock, (2) requisite approval of the Japan Financial Services Agency of an application and notification filing by Dai-ichi and its affiliates, (3) the receipt of certain insurance regulatory approvals, (4) the absence of any laws that have been adopted or promulgated, or any order, injunction, decision or decree issued or remaining in effect, that would prohibit the Merger or make the Merger illegal, and (5) the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, which waiting period terminated on July 25, 2014, pursuant to a grant of early termination by the Federal Trade Commission. Each party's obligation to consummate the Merger also is subject to certain additional conditions that include the accuracy of the other party's representations and warranties contained in the Merger Agreement (subject to certain materiality qualifiers) and the other party's compliance with its covenants and agreements contained in the Merger Agreement in all material respects. The Merger Agreement does not contain a financing condition. Subject to certain limitations, either party may terminate the Merger Agreement if the Merger is not consummated by February 28, 2015, which date is extended until April 30, 2015 in the event of delays in obtaining regulatory approval.

We expect to file a definitive proxy statement with the SEC in August 2014 which will contain detailed information about the Merger Agreement and background information regarding the transaction, and we plan to hold a special meeting of shareowners on a date to be announced at which shareowners will vote on the adoption of the Merger Agreement and the Merger. For additional information regarding the Merger and related matters, including the treatment of benefit plans, please refer to our Current Report on Form 8-K filed June 4, 2014, and Note 5, *Proposed Dai-ichi Merger*, to the consolidated condensed financial statements included in this report.

**RISKS AND UNCERTAINTIES**

The factors which could affect our future results include, but are not limited to, general economic conditions and the following risks and uncertainties:

*Risks Related to the Proposed Dai-ichi Merger*

- the Merger is subject to various closing conditions, including regulatory and third party approvals;
- failure to timely complete the Merger could adversely impact our stock price, business, financial condition, and results of operations;
- the pendency of the Merger and operating restrictions contained in the Merger Agreement could adversely affect our business and operations;
- shareowner litigation against the Company, our directors and/or Dai-ichi could delay or prevent the Merger and cause us to incur significant costs and expenses; and
- our debt ratings and the financial strength ratings of our insurance subsidiaries may be adversely affected by the transactions contemplated by the Merger Agreement;

*General*

- exposure to the risks of natural and man-made catastrophes, pandemics, malicious acts, terrorist acts and climate change, which could adversely affect our operations and results;
- a disruption affecting the electronic systems of the Company or those on whom the Company relies could adversely affect our business, financial condition and results of operations;
- confidential information maintained in our systems could be compromised or misappropriated, damaging our business and reputation and adversely affecting our financial condition and results of operations;
- our results and financial condition may be negatively affected should actual experience differ from management's assumptions and estimates;
- we may not realize our anticipated financial results from our acquisitions strategy;
- we may not be able to achieve the expected results from our recent acquisition;
- assets allocated to the MONY Closed Block benefit only the holders of certain policies; adverse performance of Closed Block assets or adverse experience of Closed Block liabilities may negatively affect us;
- we are dependent on the performance of others;
- our risk management policies, practices, and procedures could leave us exposed to unidentified or unanticipated risks, which could negatively affect our business or result in losses;
- our strategies for mitigating risks arising from our day-to-day operations may prove ineffective resulting in a material adverse effect on our results of operations and financial condition;

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*Financial environment*

- interest rate fluctuations and sustained periods of low interest rates could negatively affect our interest earnings and spread income, or otherwise impact our business;
- our investments are subject to market and credit risks, which could be heightened during periods of extreme volatility or disruption in financial and credit markets;
- equity market volatility could negatively impact our business;
- our use of derivative financial instruments within our risk management strategy may not be effective or sufficient;
- credit market volatility or disruption could adversely impact our financial condition or results from operations;
- our ability to grow depends in large part upon the continued availability of capital;
- we could be adversely affected by a ratings downgrade or other negative action by a ratings organization;
- we could be forced to sell investments at a loss to cover policyholder withdrawals;
- disruption of the capital and credit markets could negatively affect our ability to meet our liquidity and financing needs;
- difficult general economic conditions could materially adversely affect our business and results of operations;
- we may be required to establish a valuation allowance against our deferred tax assets, which could materially adversely affect our results of operations, financial condition, and capital position;
- we could be adversely affected by an inability to access our credit facility;
- we could be adversely affected by an inability to access FHLB lending;
- our financial condition or results of operations could be adversely impacted if our assumptions regarding the fair value and future performance of our investments differ from actual experience;
- the amount of statutory capital that we have and the amount of statutory capital that we must hold to maintain our financial strength and credit ratings and meet other requirements can vary significantly from time to time and is sensitive to a number of factors outside of our control;
- we operate as a holding company and depend on the ability of our subsidiaries to transfer funds to us to meet our obligations and pay dividends;

*Industry*

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- we are highly regulated, are subject to routine audits, examinations and actions by regulators, law enforcement agencies, and self-regulatory organizations;
- changes to tax law or interpretations of existing tax law could adversely affect our ability to compete with non-insurance products or reduce the demand for certain insurance products;
- financial services companies are frequently the targets of legal proceedings, including class action litigation, which could result in substantial judgments;
- publicly held companies in general and the financial services industry in particular are sometimes the target of law enforcement investigations and the focus of increased regulatory scrutiny;
- new accounting rules, changes to existing accounting rules, or the grant of permitted accounting practices to competitors could negatively impact us;
- use of reinsurance introduces variability in our statements of income;
- our reinsurers could fail to meet assumed obligations, increase rates, or be subject to adverse developments that could affect us;
- our policy claims fluctuate from period to period resulting in earnings volatility;

### *Competition*

- we operate in a mature, highly competitive industry, which could limit our ability to gain or maintain our position in the industry and negatively affect profitability;
- our ability to maintain competitive unit costs is dependent upon the level of new sales and persistency of existing business; and
- we may not be able to protect our intellectual property and may be subject to infringement claims.

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For more information about the risks, uncertainties, and other factors that could affect our future results, please see Part II, Item 1A of this report and our Annual Report on Form 10-K.

**CRITICAL ACCOUNTING POLICIES**

Our accounting policies require the use of judgments relating to a variety of assumptions and estimates, including, but not limited to expectations of current and future mortality, morbidity, persistency, expenses, and interest rates, as well as expectations around the valuations of securities. Because of the inherent uncertainty when using the assumptions and estimates, the effect of certain accounting policies under different conditions or assumptions could be materially different from those reported in the consolidated condensed financial statements. For a complete listing of our critical accounting policies, refer to our Annual Report on Form 10-K for the year ended December 31, 2013.

**RESULTS OF OPERATIONS**

We use the same accounting policies and procedures to measure segment operating income (loss) and assets as we use to measure consolidated net income and assets. Segment operating income (loss) is income before income tax, excluding realized gains and losses on investments and derivatives net of the amortization related to deferred acquisition costs ( DAC ), value of business acquired ( VOBA ), and benefits and settlement expenses. Operating earnings exclude changes in the guaranteed minimum withdrawal benefits ( GMWB ) embedded derivatives (excluding the portion attributed to economic cost), realized and unrealized gains (losses) on derivatives used to hedge the variable annuity ( VA ) product, actual GMWB incurred claims, and the related amortization of DAC attributed to each of these items.

Segment operating income (loss) represents the basis on which the performance of our business is internally assessed by management. Premiums and policy fees, other income, benefits and settlement expenses, and amortization of DAC/VOBA are attributed directly to each operating segment. Net investment income is allocated based on directly related assets required for transacting the business of that segment. Realized investment gains (losses) and other operating expenses are allocated to the segments in a manner that most appropriately reflects the operations of that segment. Investments and other assets are allocated based on statutory policy liabilities net of associated statutory policy assets, while DAC/VOBA and goodwill are shown in the segments to which they are attributable.

However, segment operating income (loss) should not be viewed as a substitute for accounting principles generally accepted in the United States of America ( GAAP ) net income. In addition, our segment operating income (loss) measures may not be comparable to similarly titled measures reported by other companies.

We periodically review and update as appropriate our key assumptions on products using the ASC Financial Services-Insurance Topic, including future mortality, expenses, lapses, premium persistency, investment yields, interest spreads, and equity market returns. Changes to these assumptions result in adjustments which increase or decrease DAC amortization and/or benefits and expenses. The periodic review and updating of assumptions is referred to as unlocking . When referring to DAC amortization or unlocking on products covered under the ASC Financial Services-Insurance Topic, the reference is to changes in all balance sheet components amortized over estimated gross profits.



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The following table presents a summary of results and reconciles segment operating income (loss) to consolidated net income:

|   | For The<br>Three Months Ended<br>June 30, |              |        | Change       | For The<br>Six Months Ended<br>June 30, |        |  | Change |
|---|---|--------------|--------|--------------|---|--------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013         |        |              | 2014<br>(Dollars In Thousands)          | 2013   |  |        |
| <b>Segment Operating Income (Loss)</b>              |   |              |        |              |   |        |  |        |
| Life Marketing                                      | \$ 26,349                                 | \$ 24,673    | 6.8%   | \$ 49,834    | \$ 48,380                               | 3.0%   |  |        |
| Acquisitions  | 64,882                                    | 29,435       | n/m    | 125,878      | 63,812                                  | 97.3   |  |        |
| Annuities   | 55,258                                    | 36,382       | 51.9   | 106,901      | 79,780                                  | 34.0   |  |        |
| Stable Value Products                               | 17,287                                    | 22,464       | (23.0) | 34,684       | 40,308                                  | (14.0) |  |        |
| Asset Protection                                    | 8,534                                     | 7,384        | 15.6   | 14,903       | 13,465                                  | 10.7   |  |        |
| Corporate and Other                                 | (12,555)                                  | (2,483)      | n/m    | (27,410)     | (20,815)                                | (31.7) |  |        |
| Total segment operating income                      | 159,755                                   | 117,855      | 35.6   | 304,790      | 224,930                                 | 35.5   |  |        |
| Realized investment gains (losses) - investments(1) | 74,920                                    | (119,311)    |        | 143,453      | (129,067)                               |        |  |        |
| Realized investment gains (losses) - derivatives    | (72,465)                                  | 158,469      |        | (160,828)    | 178,777                                 |        |  |        |
| Income tax expense                                  | (54,233)                                  | (53,814)     |        | (95,799)     | (93,150)                                |        |  |        |
| Net income  | \$ 107,977                                | \$ 103,199   | 4.6    | \$ 191,616   | \$ 181,490                              | 5.6    |  |        |
| Investment gains (losses)(2)                        | \$ 78,688                                 | \$ (113,978) |        | \$ 149,211   | \$ (122,707)                            |        |  |        |
| Less: related amortization of DAC/VOBA              | 3,768                                     | 5,333        |        | 5,758        | 6,360                                   |        |  |        |
| Realized investment gains (losses) - investments    | \$ 74,920                                 | \$ (119,311) |        | \$ 143,453   | \$ (129,067)                            |        |  |        |
| Derivative gains (losses) (3)                       | \$ (89,926)                               | \$ 143,881   |        | \$ (195,276) | \$ 151,266                              |        |  |        |
| Less: VA GMWB economic cost                         | (17,461)                                  | (14,588)     |        | (34,448)     | (27,511)                                |        |  |        |
| Realized investment gains (losses) - derivatives    | \$ (72,465)                               | \$ 158,469   |        | \$ (160,828) | \$ 178,777                              |        |  |        |

(1) Includes credit related other-than-temporary impairments of \$1.5 million and \$3.1 million for the three and six months ended June 30, 2014, respectively, as compared to \$4.0 million and \$8.6 million for the three and six months ended June 30, 2013, respectively.

(2) Includes realized investment gains (losses) before related amortization.

(3) Includes realized gains (losses) on derivatives before the VA GMWB economic cost.

***For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013***

Net income for the three months ended June 30, 2014, included a \$41.9 million, or 35.6%, increase in segment operating income. The increase consisted of a \$1.7 million increase in the Life Marketing segment, a \$35.4 million increase in the Acquisitions segment, an \$18.9 million

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increase in the Annuities segment, and a \$1.2 million increase in the Asset Protection segment. These increases were partially offset by a \$5.2 million decrease in the Stable Value Products segment and a \$10.1 million decrease in the Corporate and Other segment.

We experienced net realized losses of \$11.2 million for the three months ended June 30, 2014, as compared to net realized gains of \$29.9 million for the three months ended June 30, 2013. The losses realized for the three months ended June 30, 2014, were primarily related to \$1.5 million of other-than-temporary impairment credit-related losses, net losses of \$32.6 million on derivatives related to variable annuity contracts, net losses of \$4.7 million of derivatives related to fixed indexed annuity ( FIA ) contracts, and \$1.5 million of losses related to other investment and derivative activity. Partially offsetting these losses were gains of \$20.2 million of gains related to investment securities sale activity and \$8.8 million of gains related to the net activity of the modified coinsurance portfolio.

- Life Marketing segment operating income was \$26.3 million for the three months ended June 30, 2014, representing an increase of \$1.7 million, or 6.8%, from the three months ended June 30, 2013. The increase was primarily due to higher universal life policy fees, higher investment income, and additional revenue in the



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segment's non-insurance operations. These increases were largely offset by less favorable mortality and higher operating expenses.

- Acquisitions segment operating income was \$64.9 million for the three months ended June 30, 2014, an increase of \$35.4 million as compared to the three months ended June 30, 2013, primarily due to the impact of the MONY acquisition, which occurred in the fourth quarter of 2013. MONY operating income was \$31.2 million for the three months ended June 30, 2014.
- Annuities segment operating income was \$55.3 million for the three months ended June 30, 2014, as compared to \$36.4 million for the three months ended June 30, 2013, an increase of \$18.9 million, or 51.9%. This variance was the result of higher policy fees and other income from the variable annuities (VA) line of business along with lower credited interest, lower non-deferred expenses, and lower DAC amortization.
- Stable Value Products segment operating income was \$17.3 million and decreased \$5.2 million, or 23.0%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The decrease in operating earnings resulted from a decrease in participating mortgage income and a decline in average account values. Participating mortgage income for the three months ended June 30, 2014 was \$0.5 million compared to \$5.5 million for the three months ended June 30, 2013. The adjusted operating spread, which excludes participating income, increased by 2 basis points for the three months ended June 30, 2014 over the prior year, due primarily to a decline in credited interest.
- Asset Protection segment operating income was \$8.5 million, representing an increase of \$1.2 million, or 15.6%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Service contract earnings increased \$0.7 million primarily due to lower expenses. Credit insurance earnings increased \$0.7 million primarily due to lower losses. Earnings from the guaranteed asset protection (GAP) product line decreased \$0.3 million primarily resulting from higher losses.
- Corporate and Other segment operating loss was \$12.6 million for the three months ended June 30, 2014, as compared to an operating loss of \$2.5 million for the three months ended June 30, 2013. The decrease was primarily due to a favorable \$3.9 million guaranty fund allocation to business segments in the second quarter of 2013 and higher overhead expenses for the second quarter of 2014. In addition, the decrease was driven by a \$2.5 million decrease in mortgage loan prepayment fee income as compared to the second quarter of 2013. These decreases were partially offset by a \$2.5 million favorable variance related to gains on the repurchase of non-recourse funding obligations as compared to the three months ended June 30, 2013.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

Net income for the six months ended June 30, 2014, included a \$79.9 million, or 35.5%, increase in segment operating income. The increase consisted of a \$1.5 million increase in the Life Marketing segment, a \$62.1 million increase in the Acquisitions segment, a \$27.1 million increase in the Annuities segment, and a \$1.4 million increase in the Asset Protection segment. These increases were partially offset by a \$5.6 million decrease in the Stable Value Products segment and a \$6.6 million decrease in the Corporate and Other segment.

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We experienced net realized losses of \$46.1 million for the six months ended June 30, 2014, as compared to net realized gains of \$28.6 million for the six months ended June 30, 2013. The losses realized for the six months ended June 30, 2014, were primarily related to \$3.1 million for other-than-temporary impairment credit-related losses, net losses of \$80.8 million on derivatives related to variable annuity contracts, net losses of \$1.6 million of derivatives related to FIA contracts, and \$3.1 million of losses related to other investment and derivative activity. Partially offsetting these losses were \$27.6 million of gains related to investment securities sale activity and \$14.9 million of gains related to the net activity of the modified coinsurance portfolio.

- Life Marketing segment operating income was \$49.8 million for the six months ended June 30, 2014, representing an increase of \$1.5 million, or 3.0%, from the six months ended June 30, 2013. The increase was

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primarily due to higher universal life policy fees, higher investment income, and additional revenue in the segment's non-insurance operations. These increases were largely offset by less favorable mortality.

- Acquisitions segment operating income was \$125.9 million for the six months ended June 30, 2014, an increase of \$62.1 million, or 97.3%, as compared to the six months ended June 30, 2013, primarily due to the impact of the MONY acquisition, which occurred in the fourth quarter of 2013. MONY operating income was \$56.9 million for the six months ended June 30, 2014.
- Annuities segment operating income was \$106.9 million for the six months ended June 30, 2014, as compared to \$79.8 million for the six months ended June 30, 2013, an increase of \$27.1 million, or 34.0%. This variance was the result of higher policy fees and other income from the VA line of business along with lower credited interest, lower non-deferred expenses, and lower DAC amortization.
- Stable Value Products segment operating income was \$34.7 million and decreased \$5.6 million, or 14.0%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. The decrease in operating earnings resulted from a decrease in participating mortgage income and a decline in average account values. Participating mortgage income for the six months ended June 30, 2014 was \$1.0 million compared to \$7.2 million for the six months ended June 30, 2013. The adjusted operating spread, which excludes participating income, increased by 5 basis points for the six months ended June 30, 2014 over the prior year, due primarily to a decline in credited interest.
- Asset Protection segment operating income was \$14.9 million, representing an increase of \$1.4 million, or 10.7%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Service contract earnings increased \$1.5 million primarily due to lower expenses. Credit insurance earnings increased \$0.7 million mainly due to lower losses. Earnings from the GAP product line decreased \$0.8 million primarily due to higher losses.
- Corporate and Other segment operating loss was \$27.4 million for the six months ended June 30, 2014, as compared to an operating loss of \$20.8 million for the six months ended June 30, 2013. The decrease resulted from a decline in net investment income and an increase in other operating expenses as compared to the six months ended June 30, 2013. The decrease in net investment income was primarily driven by a \$2.6 million unfavorable variance related to mortgage loan prepayment fee income, an unfavorable variance related to income on called securities, and lower core investment income. The increase in other operating expenses was primarily due to higher overhead expenses for the six months ended June 30, 2014. These decreases were partially offset by a \$1.2 million favorable variance related to gains on the repurchase of non-recourse funding obligations.

Table of Contents**Life Marketing***Segment results of operations*

Segment results were as follows:

|   | For The<br>Three Months Ended<br>June 30, |            |        | For The<br>Six Months Ended<br>June 30, |            |        | Change |
|---|---|------------|--------|---|------------|--------|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013       | Change | 2014<br>(Dollars In Thousands)          | 2013       | Change |        |
| <b>REVENUES</b>   |   |            |        |   |            |        |        |
| Gross premiums and policy fees  | \$ 437,093                                | \$ 442,338 | (1.2)% | \$ 849,204                              | \$ 861,043 | (1.4)% |        |
| Reinsurance ceded   | (206,056)                                 | (255,180)  | 19.3   | (400,075)                               | (462,842)  | 13.6   |        |
| Net premiums and policy fees  | 231,037                                   | 187,158    | 23.4   | 449,129                                 | 398,201    | 12.8   |        |
| Net investment income   | 136,769                                   | 130,054    | 5.2    | 270,732                                 | 257,302    | 5.2    |        |
| Other income  | 30,589                                    | 29,809     | 2.6    | 63,102                                  | 59,144     | 6.7    |        |
| Total operating revenues  | 398,395                                   | 347,021    | 14.8   | 782,963                                 | 714,647    | 9.6    |        |
| Realized gains (losses) - investments(1)                                | 8,922                                     |            | n/m    | 9,120                                   |            | n/m    |        |
| Realized gains (losses) - derivatives                                   | (285)                                     |            | n/m    | (285)                                   |            | n/m    |        |
| Total revenues  | 407,032                                   | 347,021    | 17.3   | 791,798                                 | 714,647    | 10.8   |        |
| <b>BENEFITS AND EXPENSES</b>  |   |            |        |   |            |        |        |
| Benefits and settlement expenses  | 309,861                                   | 256,073    | 21.0   | 603,666                                 | 536,839    | 12.4   |        |
| Amortization of deferred policy acquisition costs                       | 17,410                                    | 27,066     | (35.7) | 41,442                                  | 41,088     | 0.9    |        |
| Other operating expenses  | 44,775                                    | 39,209     | 14.2   | 88,021                                  | 88,340     | (0.4)  |        |
| Operating benefits and settlement expenses                              | 372,046                                   | 322,348    | 15.4   | 733,129                                 | 666,267    | 10.0   |        |
| Amortization related to benefits and settlement expenses                | 1,706                                     |            | n/m    | 1,711                                   |            | n/m    |        |
| Amortization of DAC related to realized gains (losses) - investments(1) | 3,326                                     |            | n/m    | 3,355                                   |            | n/m    |        |
| Total benefits and expenses   | 377,078                                   | 322,348    | 17.0   | 738,195                                 | 666,267    | 10.8   |        |
| <b>INCOME BEFORE INCOME TAX</b>   | 29,954                                    | 24,673     | 21.4   | 53,603                                  | 48,380     | 10.8   |        |
| Less: realized gains (losses)(1)  | 8,637                                     |            |        | 8,835                                   |            |        |        |
| Less: amortization related to benefits and settlement expenses          | (1,706)                                   |            |        | (1,711)                                 |            |        |        |
| Less: related amortization of DAC(1)                                    | (3,326)                                   |            |        | (3,355)                                 |            |        |        |
| <b>OPERATING INCOME</b>   | \$ 26,349                                 | \$ 24,673  | 6.8    | \$ 49,834                               | \$ 48,380  | 3.0    |        |

(1) During the third quarter of 2013, we began allocating realized gains and losses, associated amortization of DAC, and benefits and settlement expenses to certain of our segments to better reflect the economics of the investments supporting these segments. Prior year realized gains and losses are not comparable to the current year presentation.



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The following table summarizes key data for the Life Marketing segment:

|   | For The<br>Three Months Ended<br>June 30, |                |         | Change         | For The<br>Six Months Ended<br>June 30, |      |         | Change |
|---|---|----------------|---------|----------------|---|------|---------|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013           |         |                | 2014<br>(Dollars In Thousands)          | 2013 |         |        |
| <b>Sales By Product</b>                   |   |                |         |                |   |      |         |        |
| Traditional                               | \$ 101                                    | \$ 409         | (75.3)% | \$ 250         | \$ 701                                  |      | (64.3)% |        |
| Universal life                            | 32,703                                    | 44,181         | (26.0)  | 60,884         | 91,176                                  |      | (33.2)  |        |
| BOLI                                      | 22  |                | n/m     | 22             |   |      | n/m     |        |
|   | \$ 32,826                                 | \$ 44,590      | (26.4)  | \$ 61,156      | \$ 91,877                               |      | (33.4)  |        |
| <b>Sales By Distribution Channel</b>      |   |                |         |                |   |      |         |        |
| Independent agents                        | \$ 24,843                                 | \$ 31,108      | (20.1)  | \$ 46,358      | \$ 62,645                               |      | (26.0)  |        |
| Stockbrokers / banks                      | 7,262                                     | 12,920         | (43.8)  | 13,486         | 28,223                                  |      | (52.2)  |        |
| BOLI / other                              | 721                                       | 562            | 28.3    | 1,312          | 1,009                                   |      | 30.0    |        |
|   | \$ 32,826                                 | \$ 44,590      | (26.4)  | \$ 61,156      | \$ 91,877                               |      | (33.4)  |        |
| <b>Average Life Insurance In-force(1)</b> |   |                |         |                |   |      |         |        |
| Traditional                               | \$ 405,489,033                            | \$ 430,900,880 | (5.9)   | \$ 411,306,190 | \$ 437,069,757                          |      | (5.9)   |        |
| Universal life                            | 131,860,833                               | 101,045,737    | 30.5    | 124,539,015    | 92,721,338                              |      | 34.3    |        |
|   | \$ 537,349,866                            | \$ 531,946,617 | 1.0     | \$ 535,845,205 | \$ 529,791,095                          |      | 1.1     |        |
| <b>Average Account Values</b>             |   |                |         |                |   |      |         |        |
| Universal life                            | \$ 7,146,126                              | \$ 6,866,731   | 4.1     | \$ 7,105,122   | \$ 6,737,609                            |      | 5.5     |        |
| Variable universal life                   | 549,072                                   | 446,231        | 23.0    | 526,485        | 418,999                                 |      | 25.7    |        |
|   | \$ 7,695,198                              | \$ 7,312,962   | 5.2     | \$ 7,631,607   | \$ 7,156,608                            |      | 6.6     |        |

*Operating expenses detail*

Other operating expenses for the segment were as follows:

|  | For The<br>Three Months Ended<br>June 30, |           |        | Change    | For The<br>Six Months Ended<br>June 30, |      |         | Change |
|--|---|-----------|--------|-----------|---|------|---------|--------|
|  | 2014<br>(Dollars In Thousands)            | 2013      |        |           | 2014<br>(Dollars In Thousands)          | 2013 |         |        |
| <b>Insurance companies:</b>                          |   |           |        |           |   |      |         |        |
| First year commissions                               | \$ 39,978                                 | \$ 44,190 | (9.5)% | \$ 73,045 | \$ 96,163                               |      | (24.0)% |        |
| Renewal commissions                                  | 7,884                                     | 8,573     | (8.0)  | 14,666    | 17,188                                  |      | (14.7)  |        |
| First year ceding allowances                         | (587)                                     | (1,160)   | 49.4   | (893)     | (2,095)                                 |      | 57.4    |        |
| Renewal ceding allowances                            | (25,973)                                  | (42,462)  | 38.8   | (62,816)  | (80,071)                                |      | 21.5    |        |
| General & administrative                             | 45,416                                    | 44,248    | 2.6    | 87,565    | 88,996                                  |      | (1.6)   |        |
| Taxes, licenses, and fees                            | 7,387                                     | 9,566     | (22.8) | 13,165    | 20,513                                  |      | (35.8)  |        |
| Other operating expenses incurred                    | 74,105                                    | 62,955    | 17.7   | 124,732   | 140,694                                 |      | (11.3)  |        |
| Less: commissions, allowances & expenses capitalized | (58,697)                                  | (52,410)  | (12.0) | (97,028)  | (109,728)                               |      | 11.6    |        |
|  | 15,408                                    | 10,545    | 46.1   | 27,704    | 30,966                                  |      | (10.5)  |        |

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Other insurance company  
operating expenses

|   |                  |                  |             |                  |                  |              |
|---|------------------|------------------|-------------|------------------|------------------|--------------|
| <b>Marketing companies:</b>                   |                  |                  |             |                  |                  |              |
| Commissions                                   | 21,629           | 21,018           | 2.9         | 44,650           | 42,312           | 5.5          |
| Other operating expenses                      | 7,738            | 7,646            | 1.2         | 15,667           | 15,062           | 4.0          |
| Other marketing company<br>operating expenses | 29,367           | 28,664           | 2.5         | 60,317           | 57,374           | 5.1          |
| <b>Other operating expenses</b>               | <b>\$ 44,775</b> | <b>\$ 39,209</b> | <b>14.2</b> | <b>\$ 88,021</b> | <b>\$ 88,340</b> | <b>(0.4)</b> |

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*For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013*

*Segment operating income*

Operating income was \$26.3 million for the three months ended June 30, 2014, representing an increase of \$1.7 million, or 6.8%, from the three months ended June 30, 2013. The increase was primarily due to higher universal life policy fees, higher investment income and additional revenue in the segment's non-insurance operations. These increases were largely offset by less favorable mortality and higher operating expenses.

*Operating revenues*

Total operating revenues for the three months ended June 30, 2014, increased \$51.4 million, or 14.8%, as compared to the three months ended June 30, 2013. This increase was driven by higher premiums and policy fees due to continued growth in the universal life block and the impact of unlocking on ceded premiums, which was almost entirely offset in benefit and settlement expenses. Higher investment income due to increases in net in-force reserves also contributed to the increase.

*Net premiums and policy fees*

Net premiums and policy fees increased by \$43.9 million, or 23.4%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, due to an increase in policy fees associated with continued growth in universal life business, and the impact of unlocking on ceded premiums, which was almost entirely offset in benefit and settlement expenses. This increase is partially offset by decreases in traditional life premiums.

*Net investment income*

Net investment income in the segment increased \$6.7 million, or 5.2%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Of the increase in net investment income, \$4.7 million was the result of a net increase in universal life reserves. Traditional life investment income increased \$1.5 million due to lower funding costs and higher reserves.

*Other income*



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Other income increased \$0.8 million, or 2.6%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to higher revenue in the segment's non-insurance operations.

### *Benefits and settlement expenses*

Benefits and settlement expenses increased by \$53.8 million, or 21.0%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, due to an increase in reserves and claims from growth in retained universal life insurance in-force, the impact of unlocking and higher claims due to less favorable mortality in the traditional life block. For the three months ended June 30, 2014, universal life and BOLI unlocking was largely driven by the impact of reinsurance. The impact of these changes increased benefits and settlement expenses \$25.4 million and is almost entirely offset by a decline in ceded premiums. For the three months ended June 30, 2013, universal life and BOLI unlocking decreased benefit expenses \$0.3 million.

### *Amortization of DAC*

DAC amortization decreased \$9.7 million, or 35.7%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily driven by the favorable impact of \$10.0 million in amortization expense due to reinsurance in the three months ended June 30, 2013, which was almost entirely offset in benefit and settlement expenses. For the three months ended June 30, 2014, universal life and BOLI unlocking increased amortization \$0.7 million, as compared to an increase of \$1.6 million for the three months ended June 30, 2013.

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*Other operating expenses*

Other operating expenses increased \$5.6 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. This increase reflects higher new business acquisition costs, lower traditional life ceding allowances due to fluctuations in the number of policies reaching their post level periods, higher marketing company expenses of \$0.7 million, and higher general administrative expenses of \$1.2 million. These increases were offset by the impact of unlocking on ceded premiums which was almost entirely offset in benefit and settlement expenses along with a decrease in taxes, licenses and fees of \$2.2 million.

*Sales*

Sales for the segment decreased \$11.8 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Universal life sales decreased \$11.5 million primarily due to sales in 2013 of a product we are no longer marketing.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

*Segment operating income*

Operating income was \$49.8 million for the six months ended June 30, 2014, representing an increase of \$1.5 million, or 3.0%, from the six months ended June 30, 2013. The increase was primarily due to higher universal life policy fees, higher investment income, and additional revenue in the segment's non-insurance operations. These increases were largely offset by less favorable mortality.

*Operating revenues*

Total operating revenues for the six months ended June 30, 2014, increased \$68.3 million, or 9.6%, as compared to the six months ended June 30, 2013. This increase was driven by higher premiums and policy fees due to continued growth in the universal life block and the impact of unlocking on ceded premiums, which was almost entirely offset in benefit and settlement expenses. Higher investment income due to increases in net in-force reserves also contributed to the increase, as well as additional revenue in the segment's non-insurance operations.

*Net premiums and policy fees*

Net premiums and policy fees increased by \$50.9 million, or 12.8%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, due to an increase in policy fees associated with continued growth in universal life business, and the impact of unlocking

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on ceded premiums, which was almost entirely offset in benefit and settlement expenses. This increase is partially offset by decreases in traditional life premiums.

### *Net investment income*

Net investment income in the segment increased \$13.4 million, or 5.2%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Of the increase in net investment income, \$10.2 million was the result of a net increase in universal life reserves. Traditional life investment income increased \$2.3 million due to lower funding costs and higher reserves.

### *Other income*

Other income increased \$4.0 million, or 6.7%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to higher revenue in the segment's non-insurance operations.

### *Benefits and settlement expenses*

Benefits and settlement expenses increased by \$66.8 million, or 12.4%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, due to an increase in reserves and claims from growth in retained universal life insurance in-force and higher claims due to less favorable mortality in the traditional life block.

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For the six months ended June 30, 2014, universal life and BOLI unlocking was largely driven by the impact of reinsurance and is almost entirely offset in policy fees. The impact of these changes increased benefits and settlement expenses \$21.2 million. For the six months ended June 30, 2013, universal life and BOLI unlocking increased benefit expenses \$1.6 million.

*Amortization of DAC*

DAC amortization increased \$0.4 million, or 0.9%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to the differing impacts of unlocking.

*Other operating expenses*

Other operating expenses decreased \$0.3 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. This decrease is due to the impact of unlocking on ceded premiums, almost entirely offset in benefit and settlement expenses along with lower general administrative expenses of \$1.4 million and lower taxes, licenses and fees of \$7.3 million. The decrease is largely offset by lower traditional life ceding allowances due to fluctuations in the number of policies reaching their post level periods and higher marketing company expenses of \$2.9 million.

*Sales*

Sales for the segment decreased \$30.7 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Universal life sales decreased \$30.3 million primarily due to sales in 2013 of a product we are no longer selling.

***Reinsurance***

Currently, the Life Marketing segment reinsures significant amounts of its life insurance in-force. Pursuant to the underlying reinsurance contracts, reinsurers pay allowances to the segment as a percentage of both first year and renewal premiums. Reinsurance allowances represent the amount the reinsurer is willing to pay for reimbursement of acquisition costs incurred by the direct writer of the business. A portion of reinsurance allowances received is deferred as part of DAC and a portion is recognized immediately as a reduction of other operating expenses. As the non-deferred portion of allowances reduces operating expenses in the period received, these amounts represent a net increase to operating income during that period.

Reinsurance allowances do not affect the methodology used to amortize DAC or the period over which such DAC is amortized. However, they do affect the amounts recognized as DAC amortization. DAC on universal life-type, limited-payment long duration, and investment contracts business is amortized based on the estimated gross profits of the policies in-force. Reinsurance allowances are considered in the determination of

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estimated gross profits, and therefore, impact DAC amortization on these lines of business. Deferred reinsurance allowances on level term business are recorded as ceded DAC, which is amortized over estimated ceded premiums of the policies in-force. Thus, deferred reinsurance allowances may impact DAC amortization. A more detailed discussion of the components of reinsurance can be found in the Reinsurance section of Note 2, *Summary of Significant Accounting Policies* of our Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

Table of Contents*Impact of reinsurance*

Reinsurance impacted the Life Marketing segment line items as shown in the following table:

|   | Life Marketing Segment                    |              | Line Item Impact of Reinsurance         |              |
|---|---|--------------|---|--------------|
|   | For The<br>Three Months Ended<br>June 30, |              | For The<br>Six Months Ended<br>June 30, |              |
|   | 2014                                      | 2013         | 2014                                    | 2013         |
|   | (Dollars In Thousands)                    |              |   |              |
| <b>REVENUES</b>                                   |   |              |   |              |
| Reinsurance ceded                                 | \$ (206,056)                              | \$ (255,180) | \$ (400,075)                            | \$ (462,842) |
| <b>BENEFITS AND EXPENSES</b>                      |   |              |   |              |
| Benefits and settlement expenses                  | (228,616)                                 | (266,737)    | (427,398)                               | (474,863)    |
| Amortization of deferred policy acquisition costs | (9,717)                                   | (16,992)     | (19,189)                                | (24,438)     |
| Other operating expenses (1)                      | (33,351)                                  | (37,174)     | (65,644)                                | (66,365)     |
| Total benefits and expenses                       | (271,684)                                 | (320,903)    | (512,231)                               | (565,666)    |
| <b>NET IMPACT OF REINSURANCE (2)</b>              | \$ 65,628                                 | \$ 65,723    | \$ 112,156                              | \$ 102,824   |
| Allowances received                               | \$ (26,560)                               | \$ (43,622)  | \$ (63,709)                             | \$ (79,166)  |
| Less: Amount deferred                             | (6,791)                                   | 6,448        | (1,935)                                 | 12,801       |
| Allowances recognized                             |   |              |   |              |
| (ceded other operating expenses) (1)              | \$ (33,351)                               | \$ (37,174)  | \$ (65,644)                             | \$ (66,365)  |

(1) Other operating expenses ceded per the income statement are equal to reinsurance allowances recognized after capitalization.

(2) Assumes no investment income on reinsurance. Foregone investment income would substantially reduce the favorable impact of reinsurance. The Company estimates that the impact of foregone investment income would reduce the net impact of reinsurance by 90% to 160%.

The table above does not reflect the impact of reinsurance on our net investment income. By ceding business to the assuming companies, we forgo investment income on the reserves ceded. Conversely, the assuming companies will receive investment income on the reserves assumed, which will increase the assuming companies' profitability on the business we cede. The net investment income impact to us and the assuming companies has not been quantified. The impact of including foregone investment income would be to substantially reduce the favorable net impact of reinsurance reflected above. We estimate that the impact of foregone investment income would be to reduce the net impact of reinsurance presented in the table above by 90% to 160%. The Life Marketing segment's reinsurance programs do not materially impact the other income line of our income statement.

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As shown above, reinsurance had a favorable impact on the Life Marketing segment's operating income for the periods presented above. The impact of reinsurance is largely due to our quota share coinsurance program in place prior to mid-2005. Under that program, generally 90% of the segment's traditional new business was ceded to reinsurers. Since mid-2005, a much smaller percentage of overall term business has been ceded due to a change in reinsurance strategy on traditional business. In addition, since 2012, a much smaller percentage of the segment's new universal life business has ceded. As a result of these changes, the relative impact of reinsurance on the Life Marketing segment's overall results is expected to decrease over time. While the significance of reinsurance is expected to decline over time, the overall impact of reinsurance for a given period may fluctuate due to variations in mortality, unlocking of balances, and variations from term business during the post level premium period.

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***For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013***

The lower ceded premium for 2014 as compared to 2013 was caused primarily by lower ceded traditional life premiums of \$23.6 million and universal life premiums of \$25.9 million. Ceded traditional premium for the three months ended June 30, 2014, decreased from the three months ended June 30, 2013, primarily due to fluctuations in the number of policies entering their post level period. Ceded universal life premiums for three months ended June 30, 2014, decreased from the three months ended June 30, 2013, primarily due to the impact of unlocking on ceded premiums, almost entirely offset in benefits and settlement expenses.

Ceded benefits and settlement expenses were lower for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, due to a smaller increase in ceded reserves, largely offset by higher ceded claims. Traditional ceded benefits decreased \$12.5 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to a smaller increase in post level ceded reserves, slightly offset by an increase in ceded death benefits. Universal life ceded benefits decreased \$25.5 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, due to the impact of unlocking on ceded premiums, slightly offset by an increased in ceded claims. Ceded universal life claims were \$11.7 million higher for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013.

Ceded amortization of deferred policy acquisitions costs decreased for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to the differences in unlocking between the two periods.

Ceded other operating expenses reflect the impact of reinsurance allowances on net income. Allowances decreased due to changes in the universal life reinsurance rates and the number of traditional life policies reaching their post level period.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

The lower ceded premium for 2014 as compared to 2013 was caused primarily by lower ceded traditional life premiums of \$47.2 million and lower universal life premiums of \$16.0 million. Ceded traditional premium for the six months ended June 30, 2014, decreased from the six months ended June 30, 2013, primarily due to fluctuations in the number of policies entering their post level period. Ceded universal life premiums for three months ended June 30, 2014, decreased from the six months ended June 30, 2013, primarily due to the impact of unlocking on ceded premiums, almost entirely offset in benefit and settlement expenses.

Ceded benefits and settlement expenses were lower for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, due to smaller increase in ceded reserves, partly offset by higher ceded claims. Traditional ceded benefits decreased \$43.1 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to a smaller increase in post level ceded reserves and a decrease in ceded death benefits. Universal life ceded benefits decreased \$3.7 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, due to the impact of unlocking on ceded premiums, partly offset by an increase in ceded claims. Ceded universal life claims were \$49.3 million higher for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013.



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Ceded amortization of deferred policy acquisitions costs decreased for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to the differences in unlocking between the two periods.

Ceded other operating expenses reflect the impact of reinsurance allowances on net income. Allowances decreased due to changes in the universal life reinsurance rates and the number of traditional life policies reaching their post level period.

Table of Contents**Acquisitions***Segment results of operations*

Segment results were as follows:

|   | For The<br>Three Months Ended<br>June 30, |            |  | Change | For The<br>Six Months Ended<br>June 30, |            |  | Change |
|---|---|------------|--|--------|---|------------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013       |  |        | 2014<br>(Dollars In Thousands)          | 2013       |  |        |
| <b>REVENUES</b>   |   |            |  |        |   |            |  |        |
| Gross premiums and policy fees  | \$ 305,567                                | \$ 208,194 |  | 46.8%  | \$ 601,397                              | \$ 416,920 |  | 44.2%  |
| Reinsurance ceded   | (102,346)                                 | (102,654)  |  | 0.3    | (202,715)                               | (199,259)  |  | (1.7)  |
| Net premiums and policy fees  | 203,221                                   | 105,540    |  | 92.6   | 398,682                                 | 217,661    |  | 83.2   |
| Net investment income   | 220,558                                   | 134,686    |  | 63.8   | 436,660                                 | 269,355    |  | 62.1   |
| Other income  | 3,289                                     | 1,015      |  | n/m    | 7,350                                   | 2,029      |  | n/m    |
| Total operating revenues  | 427,068                                   | 241,241    |  | 77.0   | 842,692                                 | 489,045    |  | 72.3   |
| Realized gains (losses) -<br>investments                                    | 63,530                                    | (124,691)  |  | n/m    | 134,645                                 | (138,734)  |  | n/m    |
| Realized gains (losses) -<br>derivatives                                    | (52,354)                                  | 145,143    |  | n/m    | (112,145)                               | 161,869    |  | n/m    |
| Total revenues  | 438,244                                   | 261,693    |  | 67.5   | 865,192                                 | 512,180    |  | 68.9   |
| <b>BENEFITS AND EXPENSES</b>  |   |            |  |        |   |            |  |        |
| Benefits and settlement<br>expenses   | 316,233                                   | 177,901    |  | 77.8   | 624,597                                 | 357,350    |  | 74.8   |
| Amortization of value of<br>business acquired                               | 16,341                                    | 18,661     |  | (12.4) | 34,403                                  | 36,874     |  | (6.7)  |
| Other operating expenses  | 29,612                                    | 15,244     |  | 94.3   | 57,814                                  | 31,009     |  | 86.4   |
| Operating benefits and expenses   | 362,186                                   | 211,806    |  | 71.0   | 716,814                                 | 425,233    |  | 68.6   |
| Amortization related to benefits<br>and(1) settlement expenses              | 3,531                                     |            |  | n/m    | 11,031                                  |            |  | n/m    |
| Amortization of VOBA related<br>to realized gains (losses) -<br>investments | 271                                       | 943        |  | (71.3) | 781                                     | 1,116      |  | (30.0) |
| Total benefits and expenses   | 365,988                                   | 212,749    |  | 72.0   | 728,626                                 | 426,349    |  | 70.9   |
| <b>INCOME BEFORE</b>  |   |            |  |        |   |            |  |        |
| <b>INCOME TAX</b>   | 72,256                                    | 48,944     |  | 47.6   | 136,566                                 | 85,831     |  | 59.1   |
| Less: realized gains (losses)   | 11,176                                    | 20,452     |  |        | 22,500                                  | 23,135     |  |        |
| Less: amortization related to<br>benefits settlement expenses(1)            | (3,531)                                   |            |  |        | (11,031)                                |            |  |        |
| Less: related amortization of<br>VOBA                                       | (271)                                     | (943)      |  |        | (781)                                   | (1,116)    |  |        |
| <b>OPERATING INCOME</b>   | \$ 64,882                                 | \$ 29,435  |  | n/m    | \$ 125,878                              | \$ 63,812  |  | 97.3   |

(1) During the third quarter of 2013, we began allocating benefits and settlement expenses associated with realized gains and losses to the Acquisitions segment. Prior period amounts of amortization related to benefits and settlement expenses are not comparable. Approximately \$3.6 million and \$11.2 million related to amortization of the policyholder dividend obligation related to the MONY Closed Block for the three and

six months ended June 30, 2014, respectively.

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The following table summarizes key data for the Acquisitions segment:

|   | For The<br>Three Months Ended<br>June 30, |                |  | Change | For The<br>Six Months Ended<br>June 30, |                |  | Change |
|---|---|----------------|--|--------|---|----------------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013           |  |        | 2014<br>(Dollars In Thousands)          | 2013           |  |        |
| <b>Average Life Insurance In-Force(1)</b>         |   |                |  |        |   |                |  |        |
| Traditional                                       | \$ 190,056,333                            | \$ 169,104,486 |  | 12.4%  | \$ 191,921,326                          | \$ 170,557,494 |  | 12.5%  |
| Universal life                                    | 35,310,786                                | 28,008,775     |  | 26.1   | 35,740,030                              | 28,338,399     |  | 26.1   |
|   | \$ 225,367,119                            | \$ 197,113,261 |  | 14.3   | \$ 227,661,356                          | \$ 198,895,893 |  | 14.5   |
| <b>Average Account Values</b>                     |   |                |  |        |   |                |  |        |
| Universal life                                    | \$ 4,583,381                              | \$ 3,339,818   |  | 37.2   | \$ 4,589,960                            | \$ 3,345,804   |  | 37.2   |
| Fixed annuity(2)                                  | 3,793,990                                 | 3,046,043      |  | 25.8   | 3,811,495                               | 3,064,188      |  | 25.0   |
| Variable annuity                                  | 1,503,129                                 | 576,108        |  | n/m    | 1,507,345                               | 576,064        |  | n/m    |
|   | \$ 9,880,500                              | \$ 6,961,969   |  | 42.5   | \$ 9,908,800                            | \$ 6,986,056   |  | 42.1   |
| <b>Interest Spread - UL &amp; Fixed Annuities</b> |   |                |  |        |   |                |  |        |
| Net investment income yield(3)                    | 5.71%                                     | 5.71%          |  |        | 5.67%                                   | 5.69%          |  |        |
| Interest credited to policyholders                | 3.93                                      | 4.02           |  |        | 3.94                                    | 3.97           |  |        |
| Interest spread                                   | 1.78%                                     | 1.69%          |  |        | 1.73%                                   | 1.72%          |  |        |

(1) Amounts are not adjusted for reinsurance ceded.

(2) Includes general account balances held within variable annuity products and is net of coinsurance ceded.

(3) Earned rates exclude portfolios supporting modified coinsurance and crediting rates exclude 100% cessions.

***For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013***

*Segment operating income*

Operating income was \$64.9 million for the three months ended June 30, 2014, an increase of \$35.4 million as compared to the three months ended June 30, 2013, primarily due to the impact of the MONY acquisition, which occurred in the fourth quarter of 2013. MONY operating income was \$31.2 million for the three months ended June 30, 2014.

*Operating revenues*

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Net premiums and policy fees increased \$97.7 million, or 92.6%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to the impact of the MONY acquisition, which occurred in the fourth quarter of 2013. MONY net premiums for the three months ended June 30, 2014 were \$107.5 million, and were partly offset by runoff of other business. Net investment income increased \$85.9 million, or 63.8%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, due to the \$93.4 million impact of MONY, partly offset by expected runoff of business.

### *Total benefits and expenses*

Total benefits and expenses increased \$153.2 million, or 72.0%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The increase was primarily due to the MONY acquisition, which increased operating benefits and expenses \$171.6 million.

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*For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013*

*Segment operating income*

Operating income was \$125.9 million for the six months ended June 30, 2014, an increase of \$62.1 million, or 97.3%, as compared to the six months ended June 30, 2013, primarily due to the impact of the MONY acquisition, which occurred in the fourth quarter of 2013. MONY operating income was \$56.9 million for the six months ended June 30, 2014.

*Operating revenues*

Net premiums and policy fees increased \$181.0 million, or 83.2%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to the impact of the MONY acquisition, which occurred in the fourth quarter of 2013. MONY net premiums for the six months ended June 30, 2014 were \$203.5 million, and were partly offset by runoff of other business. Net investment income increased \$167.3 million, or 62.1%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, due to the \$178.8 million impact of MONY, partly offset by expected runoff of business.

*Total benefits and expenses*

Total benefits and expenses increased \$302.3 million, or 70.9%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. The increase was primarily due to the MONY acquisition, which increased operating benefits and expenses \$330.2 million.

*Reinsurance*

The Acquisitions segment currently reinsures portions of both its life and annuity in-force. The cost of reinsurance to the segment is reflected in the chart shown below. A more detailed discussion of the components of reinsurance can be found in the Reinsurance section of Note 2, *Summary of Significant Accounting Policies* of our Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

Table of Contents*Impact of reinsurance*

Reinsurance impacted the Acquisitions segment line items as shown in the following table:

**Acquisitions Segment****Line Item Impact of Reinsurance**

|   | For The<br>Three Months Ended<br>June 30, |              | For The<br>Six Months Ended<br>June 30, |              |
|---|---|--------------|---|--------------|
|   | 2014                                      | 2013         | 2014                                    | 2013         |
|   | (Dollars In Thousands)                    |              |   |              |
| <b>REVENUES</b>                                   |   |              |   |              |
| Reinsurance ceded                                 | \$ (102,346)                              | \$ (102,654) | \$ (202,715)                            | \$ (199,259) |
| <b>BENEFITS AND EXPENSES</b>                      |   |              |   |              |
| Benefits and settlement expenses                  | (81,803)                                  | (88,074)     | (171,538)                               | (173,453)    |
| Amortization of deferred policy acquisition costs | (3,180)                                   | (2,225)      | (6,158)                                 | (4,589)      |
| Other operating expenses                          | (12,058)                                  | (12,708)     | (22,945)                                | (24,446)     |
| Total benefits and expenses                       | (97,041)                                  | (103,007)    | (200,641)                               | (202,488)    |
| <b>NET IMPACT OF REINSURANCE (1)</b>              | \$ (5,305)                                | \$ 353       | \$ (2,074)                              | \$ 3,229     |

(1) Assumes no investment income on reinsurance. Foregone investment income would substantially reduce the favorable impact of reinsurance.

The segment's reinsurance programs do not materially impact the other income line of the income statement. In addition, net investment income generally has no direct impact on reinsurance cost. However, by ceding business to the assuming companies, we forgo investment income on the reserves ceded to the assuming companies. Conversely, the assuming companies will receive investment income on the reserves assumed which will increase the assuming companies' profitability on business assumed from the Company. For business ceded under modified coinsurance arrangements, the amount of investment income attributable to the assuming company is included as part of the overall change in policy reserves and, as such, is reflected in benefit and settlement expenses. The net investment income impact to us and the assuming companies has not been quantified as it is not fully reflected in our consolidated financial statements.

The net impact of reinsurance is less favorable by \$5.7 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to lower ceded claims. In the three months ended June 30, 2014, ceded revenues decreased by \$0.3 million as the impact of the MONY acquisition largely offset normal runoff in other blocks. Ceded benefits and expenses decreased by \$6.0 million primarily due to lower claims.

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The net impact of reinsurance is less favorable by \$5.3 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to lower ceded claims excluding the impact of MONY and a recapture in 2013. In the six months ended June 30, 2014, ceded revenues increased by \$3.5 million as the impact of the MONY acquisition more than offset the impact of runoff and a recapture in 2013. Ceded benefits and expenses decreased by \$1.8 million as the impact of runoff and a 2013 recapture more than offset the impact of the MONY acquisition.



Table of Contents**Annuities****Segment results of operations**

Segment results were as follows:

|  | For The<br>Three Months Ended<br>June 30, |           |        | Change    | For The<br>Six Months Ended<br>June 30, |        |  | Change |
|--|---|-----------|--------|-----------|---|--------|--|--------|
|  | 2014<br>(Dollars In Thousands)            | 2013      |        |           | 2014<br>(Dollars In Thousands)          | 2013   |  |        |
| <b>REVENUES</b>  |   |           |        |           |   |        |  |        |
| Gross premiums and policy fees   | \$ 37,559                                 | \$ 32,965 | 13.9%  | \$ 73,831 | \$ 61,517                               | 20.0%  |  |        |
| Reinsurance ceded  |   |           | n/m    |           |   | n/m    |  |        |
| Net premiums and policy fees   | 37,559                                    | 32,965    | 13.9   | 73,831    | 61,517                                  | 20.0   |  |        |
| Net investment income  | 116,831                                   | 116,789   | n/m    | 234,297   | 235,346                                 | (0.4)  |  |        |
| Realized gains (losses) -<br>derivatives   | (17,461)                                  | (14,588)  | (19.7) | (34,448)  | (27,511)                                | (25.2) |  |        |
| Other income   | 35,987                                    | 30,600    | 17.6   | 71,417    | 57,395                                  | 24.4   |  |        |
| Total operating revenues   | 172,916                                   | 165,766   | 4.3    | 345,097   | 326,747                                 | 5.6    |  |        |
| Realized gains (losses) -<br>investments   | 2,338                                     | 8,218     | (71.6) | 2,947     | 9,991                                   | (70.5) |  |        |
| Realized gains (losses) -<br>derivatives, net of economic<br>cost                      | (19,837)                                  | 12,041    | n/m    | (47,970)  | 14,216                                  | n/m    |  |        |
| Total revenues   | 155,417                                   | 186,025   | (16.5) | 300,074   | 350,954                                 | (14.5) |  |        |
| <b>BENEFITS AND EXPENSES</b>   |   |           |        |           |   |        |  |        |
| Benefits and settlement<br>expenses  | 76,974                                    | 82,170    | (6.3)  | 154,833   | 162,841                                 | (4.9)  |  |        |
| Amortization of deferred policy<br>acquisition costs and value of<br>business acquired | 11,796                                    | 15,763    | (25.2) | 26,168    | 26,417                                  | (0.9)  |  |        |
| Other operating expenses   | 28,888                                    | 31,451    | (8.1)  | 57,195    | 57,709                                  | (0.9)  |  |        |
| Operating benefits and expenses  | 117,658                                   | 129,384   | (9.1)  | 238,196   | 246,967                                 | (3.6)  |  |        |
| Amortization related to benefits<br>and settlement expenses                            | (226)                                     | (255)     | 11.4   | 2,007     | (856)                                   | n/m    |  |        |
| Amortization of DAC related to<br>realized gains (losses) -<br>investments             | (4,840)                                   | 4,645     | n/m    | (13,127)  | 6,100                                   | n/m    |  |        |
| Total benefits and expenses  | 112,592                                   | 133,774   | (15.8) | 227,076   | 252,211                                 | (10.0) |  |        |
| <b>INCOME BEFORE INCOME<br/>TAX</b>  |   |           |        |           |   |        |  |        |
|  | 42,825                                    | 52,251    | (18.0) | 72,998    | 98,743                                  | (26.1) |  |        |
| Less: realized gains (losses) -<br>investments   | 2,338                                     | 8,218     |        | 2,947     | 9,991                                   |        |  |        |
| Less: realized gains (losses) -<br>derivatives, net of economic<br>cost                | (19,837)                                  | 12,041    |        | (47,970)  | 14,216                                  |        |  |        |
| Less: amortization related to<br>benefits and settlement expenses                      | 226                                       | 255       |        | (2,007)   | 856                                     |        |  |        |

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Less: related amortization of

|                         |                  |                  |             |                   |                  |             |  |
|-------------------------|------------------|------------------|-------------|-------------------|------------------|-------------|--|
| DAC                     | 4,840            | (4,645)          |             | 13,127            | (6,100)          |             |  |
| <b>OPERATING INCOME</b> | <b>\$ 55,258</b> | <b>\$ 36,382</b> | <b>51.9</b> | <b>\$ 106,901</b> | <b>\$ 79,780</b> | <b>34.0</b> |  |

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The following table summarizes key data for the Annuities segment:

|   | For The<br>Three Months Ended<br>June 30, |               |        | Change        | For The<br>Six Months Ended<br>June 30, |        |  | Change |
|---|---|---------------|--------|---------------|---|--------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013          |        |               | 2014<br>(Dollars In Thousands)          | 2013   |  |        |
| <b>Sales</b>                                |   |               |        |               |   |        |  |        |
| Fixed annuity                               | \$ 213,601                                | \$ 138,098    | 54.7%  | \$ 449,755    | \$ 253,451                              | 77.5%  |  |        |
| Variable annuity                            | 227,303                                   | 718,884       | (68.4) | 407,508       | 1,298,582                               | (68.6) |  |        |
|   | \$ 440,904                                | \$ 856,982    | (48.6) | \$ 857,263    | \$ 1,552,033                            | (44.8) |  |        |
| <b>Average Account Values</b>               |   |               |        |               |   |        |  |        |
| Fixed annuity(1)                            | \$ 8,213,004                              | \$ 8,362,307  | (1.8)  | \$ 8,197,573  | \$ 8,379,059                            | (2.2)  |  |        |
| Variable annuity                            | 12,314,739                                | 10,474,221    | 17.6   | 12,174,897    | 10,037,472                              | 21.3   |  |        |
|   | \$ 20,527,743                             | \$ 18,836,528 | 9.0    | \$ 20,372,470 | \$ 18,416,531                           | 10.6   |  |        |
| <b>Interest Spread - Fixed Annuities(2)</b> |   |               |        |               |   |        |  |        |
| Net investment income yield                 | 5.46%                                     | 5.48%         |        | 5.48%         | 5.51%                                   |        |  |        |
| Interest credited to policyholders          | 3.35                                      | 3.57          |        | 3.35          | 3.56                                    |        |  |        |
| Interest spread                             | 2.11%                                     | 1.91%         |        | 2.13%         | 1.95%                                   |        |  |        |

(1) Includes general account balances held within variable annuity products.

(2) Interest spread on average general account values.

|   | For The<br>Three Months Ended<br>June 30, |            |           | Change    | For The<br>Six Months Ended<br>June 30, |           |  | Change |
|---|---|------------|-----------|-----------|---|-----------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013       |           |           | 2014<br>(Dollars In Thousands)          | 2013      |  |        |
| <b>Derivatives related to variable annuity contracts:</b> |   |            |           |           |   |           |  |        |
| Interest rate futures - VA                                | \$ 6,548                                  | \$ (7,654) | \$ 14,202 | \$ 10,798 | \$ (24,138)                             | \$ 34,936 |  |        |
| Equity futures - VA                                       | (7,259)                                   | (4,036)    | (3,223)   | (9,910)   | (27,261)                                | 17,351    |  |        |
| Currency futures - VA                                     | (2,887)                                   | (112)      | (2,775)   | (4,165)   | 7,971                                   | (12,136)  |  |        |
| Variance swaps - VA                                       | (823)                                     | 2,214      | (3,037)   | (2,673)   | (8,219)                                 | 5,546     |  |        |
| Equity options - VA                                       | (20,949)                                  | (8,131)    | (12,818)  | (33,290)  | (36,537)                                | 3,247     |  |        |
| Interest rate swaptions - VA                              | (4,998)                                   | 1,639      | (6,637)   | (14,401)  | (2,463)                                 | (11,938)  |  |        |
| Interest rate swaps - VA                                  | 45,169                                    | (89,722)   | 134,891   | 102,537   | (106,278)                               | 208,815   |  |        |
| Embedded derivative - GMWB(1)                             | (47,389)                                  | 103,315    | (150,704) | (129,676) | 183,690                                 | (313,366) |  |        |
| Total derivatives related to variable annuity contracts   | (32,588)                                  | (2,487)    | (30,101)  | (80,780)  | (13,235)                                | (67,545)  |  |        |
| <b>Derivatives related to FIA contracts:</b>              |   |            |           |           |   |           |  |        |
| Embedded derivative - FIA                                 | (8,307)                                   | (41)       | (8,266)   | (6,574)   | (41)                                    | (6,533)   |  |        |
| Equity futures - FIA                                      | 605                                       |            | 605       | 950       |   | 950       |  |        |
| Volatility futures - FIA                                  | 8   |            | 8         | 8         |   | 8         |  |        |
| Equity options - FIA                                      | 2,984                                     | (19)       | 3,003     | 3,978     | (19)                                    | 3,997     |  |        |
|   | (4,710)                                   | (60)       | (4,650)   | (1,638)   | (60)                                    | (1,578)   |  |        |

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Total derivatives related to

FIA contracts

|   |             |           |             |             |           |             |
|---|-------------|-----------|-------------|-------------|-----------|-------------|
| VA GMWB economic cost(2)  | 17,461      | 14,588    | 2,873       | 34,448      | 27,511    | 6,937       |
| Realized gains (losses) -<br>derivatives, net of economic<br>cost | \$ (19,837) | \$ 12,041 | \$ (31,878) | \$ (47,970) | \$ 14,216 | \$ (62,186) |

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(1) Includes impact of nonperformance risk of \$(6.9) million and \$(10.0) million for the three and six months ended June 30, 2014 and \$12.8 million and \$7.4 million for the three and six months ended June 30, 2013, respectively.

(2) Economic cost is the long-term expected average cost of providing the product benefit over the life of the policy based on product pricing assumptions. These include assumptions about the economic/market environment, and elective and non-elective policy owner behavior (e.g. lapses, withdrawal timing, mortality, etc.).

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|  | June 30, 2014          | As of<br>December 31, 2013 | Change |
|--|------------------------|----------------------------|--------|
|  | (Dollars In Thousands) |                            |        |
| <b>GMDB - Net amount at risk(1)</b>        | \$ 83,410              | \$ 90,021                  | (7.3)% |
| <b>GMDB Reserves</b>                       | 17,118                 | 16,001                     | 7.0    |
| <b>GMWB and GMAB Reserves</b>              | (26,552)               | 156,228                    | n/m    |
| <b>Account value subject to GMWB rider</b> | 9,902,234              | 9,513,847                  | 4.1    |
| <b>GMWB Benefit Base</b>                   | 9,575,392              | 9,162,797                  | 4.5    |
| <b>GMAB Benefit Base</b>                   | 5,020                  | 5,441                      | (7.7)  |
| <b>S&amp;P 500® Index</b>                  | 1,960                  | 1,848                      | 6.1    |

(1) Guaranteed benefits in excess of contract holder account balance.

***For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013****Segment operating income*

Segment operating income was \$55.3 million for the three months ended June 30, 2014, as compared to \$36.4 million for the three months ended June 30, 2013, an increase of \$18.9 million, or 51.9%. This variance was the result of higher policy fees and other income from the VA line of business along with lower credited interest, lower non-deferred expenses, and lower DAC amortization.

*Operating revenues*

Segment operating revenues increased \$7.2 million, or 4.3%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to increases in policy fees and other income from the VA line of business. Those increases were partially offset by increased GMWB economic cost in the VA line of business. Average fixed account balances decreased 1.8% and average variable account balances grew 17.6% for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013.

*Benefits and settlement expenses*

Benefits and settlement expenses decreased \$5.2 million, or 6.3%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. This decrease was primarily the result of lower credited interest, lower realized losses in the fixed market value adjusted ( MVA ) annuities line, and lower amortization. These favorable changes were partially offset by a \$0.4 million unfavorable change in fixed indexed annuities ( FIA ) fair value adjustments and a \$0.6 million unfavorable change in the single premium immediate annuity ( SPIA ) mortality variance.

*Amortization of DAC*

DAC amortization decreased \$4.0 million, or 25.2%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The decrease was primarily due to a \$3.2 million favorable change in unlocking. DAC unlocking for the three months ended June 30, 2014 was \$3.2 million favorable, as compared to an immaterial amount of favorable unlocking for the three months ended June 30, 2013.

*Other operating expenses*

Other operating expenses decreased \$2.6 million, or 8.1%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The decrease is primarily due to a favorable change of \$2.7 million on guaranty fund assessments. Increases in non-deferred commissions were offset by lower acquisition, maintenance, and overhead expenses.

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*Sales*

Total sales decreased \$416.1 million, or 48.6%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Sales of variable annuities decreased \$491.6 million, or 68.4% for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Sales of fixed annuities increased by \$75.5 million, or 54.7%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, driven by an increase in FIA sales.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

*Segment operating income*

Segment operating income was \$106.9 million for the six months ended June 30, 2014, as compared to \$79.8 million for the six months ended June 30, 2013, an increase of \$27.1 million, or 34.0%. This variance was the result of higher policy fees and other income from the VA line of business along with lower credited interest, lower non-deferred expenses, and lower DAC amortization.

*Operating revenues*

Segment operating revenues increased \$18.4 million, or 5.6%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to increases in policy fees and other income from the VA line of business. Those increases were partly offset by increased GMWB economic cost in the VA line of business and lower investment income. Average fixed account balances decreased 2.2% and average variable account balances grew 21.3% for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013.

*Benefits and settlement expenses*

Benefits and settlement expenses decreased \$8.0 million, or 4.9%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. This decrease was primarily the result of lower credited interest, lower realized losses in the MVA annuities line and lower amortization. These favorable changes were partially offset by an unfavorable variance in the change in VA guaranteed benefit reserves and a \$2.2 million unfavorable change in the SPIA mortality variance.

*Amortization of DAC*

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DAC amortization decreased \$0.2 million, or 0.9%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to the impact of unlocking. DAC unlocking for the six months ended June 30, 2014 was \$4.5 million favorable, as compared to \$4.1 million of favorable unlocking for the six months ended June 30, 2013.

### *Other operating expenses*

Other operating expenses decreased \$0.5 million, or 0.9%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. The decrease is due to a favorable change of \$2.7 million on guaranty fund assessments along with lower acquisition, maintenance, and overhead expenses. These favorable variances were partially offset by higher commissions in the VA line of business.

### *Sales*

Total sales decreased \$694.8 million, or 44.8%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Sales of variable annuities decreased \$891.1 million, or 68.6% for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Sales of fixed annuities increased by \$196.3 million, or 77.5% for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, driven by an increase in FIA sales.



Table of Contents**Stable Value Products***Segment results of operations*

Segment results were as follows:

|   | For The<br>Three Months Ended<br>June 30, |           |         | Change    | For The<br>Six Months Ended<br>June 30, |         |  | Change |
|---|---|-----------|---------|-----------|---|---------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013      |         |           | 2014<br>(Dollars In Thousands)          | 2013    |  |        |
| <b>REVENUES</b>                                   |   |           |         |           |   |         |  |        |
| Net investment income                             | \$ 27,178                                 | \$ 33,651 | (19.2)% | \$ 54,956 | \$ 63,725                               | (13.8)% |  |        |
| Other income                                      | 1   |           | n/m     | 1         |   | n/m     |  |        |
| Total operating revenues                          | 27,179                                    | 33,651    | (19.2)  | 54,957    | 63,725                                  | (13.8)  |  |        |
| Realized gains (losses)                           | (70)                                      | 817       | n/m     | (29)      | 2,663                                   | n/m     |  |        |
| Total revenues                                    | 27,109                                    | 34,468    | (21.4)  | 54,928    | 66,388                                  | (17.3)  |  |        |
| <b>BENEFITS AND EXPENSES</b>                      |   |           |         |           |   |         |  |        |
| Benefits and settlement expenses                  | 9,525                                     | 10,683    | (10.8)  | 19,333    | 22,286                                  | (13.3)  |  |        |
| Amortization of deferred policy acquisition costs | 99  | 96        | 3.1     | 199       | 177                                     | 12.4    |  |        |
| Other operating expenses                          | 268                                       | 408       | (34.3)  | 741       | 954                                     | (22.3)  |  |        |
| Total benefits and expenses                       | 9,892                                     | 11,187    | (11.6)  | 20,273    | 23,417                                  | (13.4)  |  |        |
| <b>INCOME BEFORE INCOME TAX</b>                   |   |           |         |           |   |         |  |        |
|   | 17,217                                    | 23,281    | (26.0)  | 34,655    | 42,971                                  | (19.4)  |  |        |
| Less: realized gains (losses)                     | (70)                                      | 817       |         | (29)      | 2,663                                   |         |  |        |
| <b>OPERATING INCOME</b>                           | \$ 17,287                                 | \$ 22,464 | (23.0)  | \$ 34,684 | \$ 40,308                               | (14.0)  |  |        |

The following table summarizes key data for the Stable Value Products segment:

|                               | For The<br>Three Months Ended<br>June 30, |              |        | Change       | For The<br>Six Months Ended<br>June 30, |        |  | Change |
|-------------------------------|---|--------------|--------|--------------|---|--------|--|--------|
|                               | 2014<br>(Dollars In Thousands)            | 2013         |        |              | 2014<br>(Dollars In Thousands)          | 2013   |  |        |
| <b>Sales</b>                  |   |              |        |              |   |        |  |        |
| GIC                           | \$  | \$ 205,284   | n/m%   | \$ 25,850    | \$ 317,304                              | n/m%   |  |        |
| GFA - Direct Institutional    | 50,000                                    |              | n/m    | 50,000       |   | n/m    |  |        |
|                               | \$ 50,000                                 | \$ 205,284   | (75.6) | \$ 75,850    | \$ 317,304                              | (76.1) |  |        |
| <b>Average Account Values</b> |   |              |        |              |   |        |  |        |
|                               | \$ 2,498,395                              | \$ 2,542,096 | (1.7)% | \$ 2,538,995 | \$ 2,542,987                            | (0.2)% |  |        |
| <b>Ending Account Values</b>  | \$ 2,435,995                              | \$ 2,579,172 | (5.6)% | \$ 2,435,995 | \$ 2,579,172                            | (5.6)% |  |        |
| <b>Operating Spread</b>       |   |              |        |              |   |        |  |        |
| Net investment income yield   | 4.35%                                     | 5.29%        |        | 4.33%        | 5.01%                                   |        |  |        |
| Interest credited             | 1.52                                      | 1.68         |        | 1.52         | 1.75                                    |        |  |        |

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|                              |       |       |       |       |
|------------------------------|-------|-------|-------|-------|
| Operating expenses           | 0.06  | 0.08  | 0.08  | 0.09  |
| Operating spread             | 2.77% | 3.53% | 2.73% | 3.17% |
| Adjusted operating spread(1) | 2.69% | 2.67% | 2.66% | 2.61% |

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(1) Excludes participating mortgage loan income and other income.

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***For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013***

*Segment operating income*

Operating income was \$17.3 million and decreased \$5.2 million, or 23.0%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The decrease in operating earnings resulted from a decrease in participating mortgage income and a decline in average account values. Participating mortgage income for the three months ended June 30, 2014 was \$0.5 million compared to \$5.5 million for the three months ended June 30, 2013. The adjusted operating spread, which excludes participating income, increased by 2 basis points for the three months ended June 30, 2014 over the prior year, due primarily to a decline in credited interest.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

*Segment operating income*

Operating income was \$34.7 million and decreased \$5.6 million, or 14.0%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. The decrease in operating earnings resulted from a decrease in participating mortgage income and a decline in average account values. Participating mortgage income for the six months ended June 30, 2014 was \$1.0 million compared to \$7.2 million for the six months ended June 30, 2013. The adjusted operating spread, which excludes participating income, increased by 5 basis points for the six months ended June 30, 2014 over the prior year, due primarily to a decline in credited interest.

Table of Contents**Asset Protection***Segment results of operations*

Segment results were as follows:

|   | For The<br>Three Months Ended<br>June 30, |           |  | Change | For The<br>Six Months Ended<br>June 30, |            |  | Change |
|---|---|-----------|--|--------|---|------------|--|--------|
|   | 2014<br>(Dollars In Thousands)            | 2013      |  |        | 2014<br>(Dollars In Thousands)          | 2013       |  |        |
| <b>REVENUES</b>                                   |   |           |  |        |   |            |  |        |
| Gross premiums and policy fees                    | \$ 67,438                                 | \$ 68,203 |  | (1.1)% | \$ 134,712                              | \$ 134,389 |  | 0.2%   |
| Reinsurance ceded                                 | (34,561)                                  | (32,652)  |  | (5.8)  | (67,885)                                | (63,735)   |  | (6.5)  |
| Net premiums and policy fees                      | 32,877                                    | 35,551    |  | (7.5)  | 66,827                                  | 70,654     |  | (5.4)  |
| Net investment income                             | 5,725                                     | 5,782     |  | (1.0)  | 11,454                                  | 11,636     |  | (1.6)  |
| Other income                                      | 32,268                                    | 30,480    |  | 5.9    | 58,972                                  | 57,094     |  | 3.3    |
| Total operating revenues                          | 70,870                                    | 71,813    |  | (1.3)  | 137,253                                 | 139,384    |  | (1.5)  |
| <b>BENEFITS AND EXPENSES</b>                      |   |           |  |        |   |            |  |        |
| Benefits and settlement expenses                  | 24,448                                    | 25,964    |  | (5.8)  | 49,068                                  | 50,622     |  | (3.1)  |
| Amortization of deferred policy acquisition costs | 7,004                                     | 7,607     |  | (7.9)  | 13,649                                  | 15,069     |  | (9.4)  |
| Other operating expenses                          | 30,884                                    | 30,858    |  | 0.1    | 59,633                                  | 60,228     |  | (1.0)  |
| Total benefits and expenses                       | 62,336                                    | 64,429    |  | (3.2)  | 122,350                                 | 125,919    |  | (2.8)  |
| <b>INCOME BEFORE INCOME TAX</b>                   |   |           |  |        |   |            |  |        |
|   | 8,534                                     | 7,384     |  | 15.6   | 14,903                                  | 13,465     |  | 10.7   |
| <b>OPERATING INCOME</b>                           | \$ 8,534                                  | \$ 7,384  |  | 15.6   | \$ 14,903                               | \$ 13,465  |  | 10.7   |

The following table summarizes key data for the Asset Protection segment:

|                       | For The<br>Three Months Ended<br>June 30, |            |  | Change  | For The<br>Six Months Ended<br>June 30, |            |  | Change  |
|-----------------------|---|------------|--|---------|---|------------|--|---------|
|                       | 2014<br>(Dollars In Thousands)            | 2013       |  |         | 2014<br>(Dollars In Thousands)          | 2013       |  |         |
| <b>Sales</b>          |   |            |  |         |   |            |  |         |
| Credit insurance      | \$ 8,216                                  | \$ 9,852   |  | (16.6)% | \$ 15,058                               | \$ 17,186  |  | (12.4)% |
| Service contracts     | 102,335                                   | 99,153     |  | 3.2     | 184,247                                 | 181,188    |  | 1.7     |
| GAP                   | 19,011                                    | 17,453     |  | 8.9     | 35,758                                  | 32,219     |  | 11.0    |
|                       | \$ 129,562                                | \$ 126,458 |  | 2.5     | \$ 235,063                              | \$ 230,593 |  | 1.9     |
| <b>Loss Ratios(1)</b> |   |            |  |         |   |            |  |         |
| Credit insurance      | 16.1%                                     | 44.1%      |  |         | 28.6%                                   | 41.8%      |  |         |
| Service contracts     | 90.5                                      | 91.0       |  |         | 86.9                                    | 88.6       |  |         |
| GAP                   | 57.9                                      | 39.8       |  |         | 58.1                                    | 39.6       |  |         |

- (1) Incurred claims as a percentage of earned premiums

*For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013*

*Segment operating income*

Operating income was \$8.5 million, representing an increase of \$1.2 million, or 15.6%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Service contract earnings increased \$0.7 million primarily due to lower expenses. Credit insurance earnings increased \$0.7 million primarily due to lower losses. Earnings from the GAP product line decreased \$0.3 million primarily resulting from higher losses.

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*Net premiums and policy fees*

Net premiums and policy fees decreased \$2.7 million, or 7.5%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Service contract premiums decreased \$1.3 million and GAP premiums decreased \$0.8 million primarily due to higher ceded premiums. Credit insurance premiums decreased \$0.6 million as a result of lower sales.

*Other income*

Other income increased \$1.8 million, or 5.9%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013 due primarily to higher volume in the service contract and GAP lines.

*Benefits and settlement expenses*

Benefits and settlement expenses decreased \$1.5 million, or 5.8%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Service contract claims decreased \$1.3 million due primarily to higher ceded claims, while credit insurance claims decreased \$1.3 million due to lower loss ratios. The decreases were partially offset by an increase in GAP claims of \$1.1 million due to a higher loss ratio.

*Amortization of DAC and Other operating expenses*

Amortization of DAC was \$0.6 million, or 7.9%, lower for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to lower earned premiums in the GAP and credit product lines. Other operating expenses remained consistent with the prior year.

*Sales*

Total segment sales increased \$3.1 million, or 2.5%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. Higher auto sales helped drive increased service contract sales of \$3.2 million and higher GAP sales of \$1.6 million. Credit insurance sales decreased \$1.6 million due to decreasing demand for the product.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

*Segment operating income*

Operating income was \$14.9 million, representing an increase of \$1.4 million, or 10.7%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Service contract earnings increased \$1.5 million primarily due to lower expenses. Credit insurance earnings increased \$0.7 million mainly due to lower losses. Earnings from the GAP product line decreased \$0.8 million primarily due higher losses.

*Net premiums and policy fees*

Net premiums and policy fees decreased \$3.8 million, or 5.4%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Service contract premiums decreased \$2.3 million and GAP premiums decreased \$1.9 million primarily due to higher ceded premiums. The decreases were partially offset by an increase in credit insurance premiums of \$0.4 million.

*Other income*

Other income increased \$1.9 million, or 3.3%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013 due primarily to higher volume in the service contract and GAP lines.

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*Benefits and settlement expenses*

Benefits and settlement expenses decreased \$1.6 million, or 3.1%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Service contract claims decreased \$2.9 million due primarily to higher ceded claims, while credit insurance claims decreased \$0.8 million due to lower loss ratios. The decreases were partially offset by an increase in GAP claims of \$2.1 million due to a higher loss ratio.

*Amortization of DAC and Other operating expenses*

Amortization of DAC was \$1.4 million, or 9.4%, lower for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to lower earned premiums in the GAP product line. Other operating expenses decreased \$0.6 million, or 1.0%, for the six months ended June 30, 2014.

*Sales*

Total segment sales increased \$4.5 million, or 1.9%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Higher auto sales helped drive increased GAP sales of \$3.5 million and higher service contract sales of \$3.1 million. The increases were partially offset by a decrease in credit insurance sales of \$2.1 million due to decreasing demand for the product.

*Reinsurance*

The majority of the Asset Protection segment's reinsurance activity relates to the cession of single premium credit life and credit accident and health insurance, vehicle service contracts, and guaranteed asset protection insurance to producer affiliated reinsurance companies ( PARCs ). These arrangements are coinsurance contracts ceding the business on a first dollar quota share basis at 100% to limit our exposure and allow the PARCs to share in the underwriting income of the product. Reinsurance contracts do not relieve us from our obligations to our policyholders. A more detailed discussion of the components of reinsurance can be found in the Reinsurance section of Note 2, *Summary of Significant Accounting Policies* to our Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

Reinsurance impacted the Asset Protection segment line items as shown in the following table:

**Asset Protection Segment**

**Line Item Impact of Reinsurance**



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|   | For The<br>Three Months Ended<br>June 30, |             | For The<br>Six Months Ended<br>June 30, |             |
|---|---|-------------|---|-------------|
|   | 2014                                      | 2013        | 2014                                    | 2013        |
|   | (Dollars In Thousands)                    |             |   |             |
| <b>REVENUES</b>                                   |   |             |   |             |
| Reinsurance ceded                                 | \$ (34,561)                               | \$ (32,652) | \$ (67,885)                             | \$ (63,735) |
| <b>BENEFITS AND EXPENSES</b>                      |   |             |   |             |
| Benefits and settlement expenses                  | (16,331)                                  | (14,245)    | (30,760)                                | (27,901)    |
| Amortization of deferred policy acquisition costs | (1,259)                                   | (1,768)     | (3,038)                                 | (3,422)     |
| Other operating expenses                          | (2,097)                                   | (1,653)     | (3,672)                                 | (2,964)     |
| Total benefits and expenses                       | (19,687)                                  | (17,666)    | (37,470)                                | (34,287)    |
| <b>NET IMPACT OF REINSURANCE (1)</b>              | \$ (14,874)                               | \$ (14,986) | \$ (30,415)                             | \$ (29,448) |

(1) Assumes no investment income on reinsurance. Foregone investment income would substantially change the impact of reinsurance.

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***For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013***

Reinsurance premiums ceded increased \$1.9 million, or 5.8%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The increase was primarily due to an increase in ceded service contract premiums.

Benefits and settlement expenses ceded increased \$2.1 million, or 14.6%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The increase was primarily due to higher ceded losses in the service contract and GAP product lines.

Amortization of DAC ceded decreased \$0.5 million, mostly offset by increases in other operating expenses of \$0.4 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily as the result of ceded activity in the GAP product line.

Net investment income has no direct impact on reinsurance cost. However, by ceding business to the assuming companies, we forgo investment income on the reserves ceded. Conversely, the assuming companies will receive investment income on the reserves assumed which generally will increase the assuming companies' profitability on business we cede. The net investment income impact to us and the assuming companies has not been quantified as it is not reflected in our consolidated financial statements.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

Reinsurance premiums ceded increased \$4.2 million, or 6.5%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. Increases in ceded premiums in the GAP and service contract lines were offset by decreases in ceded premiums in the dealer credit line.

Benefits and settlement expenses ceded increased \$2.9 million, or 10.2%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. The increase was primarily due to higher ceded losses in the service contract and GAP product line.

Amortization of DAC ceded decreased \$0.4 million, offset by increases in other operating expenses of \$0.7 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily as the result of ceded activity in the GAP product lines.

Net investment income has no direct impact on reinsurance cost. However, by ceding business to the assuming companies, we forgo investment income on the reserves ceded. Conversely, the assuming companies will receive investment income on the reserves assumed which generally will increase the assuming companies' profitability on business we cede. The net investment income impact to us and the assuming companies has not been quantified as it is not reflected in our consolidated financial statements.



Table of Contents**Corporate and Other***Segment results of operations*

Segment results were as follows:

|  | For The<br>Three Months Ended<br>June 30, |            |         | Change      | For The<br>Six Months Ended<br>June 30, |        |  | Change |
|--|---|------------|---------|-------------|---|--------|--|--------|
|  | 2014<br>(Dollars In Thousands)            | 2013       |         |             | 2014<br>(Dollars In Thousands)          | 2013   |  |        |
| <b>REVENUES</b>                                      |   |            |         |             |   |        |  |        |
| Gross premiums and policy fees                       | \$ 4,145                                  | \$ 4,631   | (10.5)% | \$ 8,554    | \$ 9,309                                | (8.1)% |  |        |
| Reinsurance ceded                                    | (5)                                       | (4)        | (25.0)  | (6)         | (4)                                     | (50.0) |  |        |
| Net premiums and policy fees                         | 4,140                                     | 4,627      | (10.5)  | 8,548       | 9,305                                   | (8.1)  |  |        |
| Net investment income                                | 43,755                                    | 45,258     | (3.3)   | 80,880      | 86,490                                  | (6.5)  |  |        |
| Other income   | 4,797                                     | 2,488      | 92.8    | 5,128       | 3,757                                   | 36.5   |  |        |
| Total operating revenues                             | 52,692                                    | 52,373     | 0.6     | 94,556      | 99,552                                  | (5.0)  |  |        |
| Realized gains (losses) -<br>investments             | 3,803                                     | 1,120      | n/m     | 2,402       | 3,183                                   | (24.5) |  |        |
| Realized gains (losses) -<br>derivatives             | 176                                       | 1,843      | (90.5)  | (302)       | 2,882                                   | n/m    |  |        |
| Total revenues                                       | 56,671                                    | 55,336     | 2.4     | 96,656      | 105,617                                 | (8.5)  |  |        |
| <b>BENEFITS AND EXPENSES</b>                         |   |            |         |             |   |        |  |        |
| Benefits and settlement expenses                     | 5,764                                     | 5,330      | 8.1     | 10,089      | 10,664                                  | (5.4)  |  |        |
| Amortization of deferred policy<br>acquisition costs | 124                                       | 165        | (24.8)  | 243         | 344                                     | (29.4) |  |        |
| Other operating expenses                             | 59,359                                    | 49,361     | 20.3    | 111,634     | 109,359                                 | 2.1    |  |        |
| Total benefits and expenses                          | 65,247                                    | 54,856     | 18.9    | 121,966     | 120,367                                 | 1.3    |  |        |
| <b>INCOME (LOSS) BEFORE<br/>INCOME TAX</b>           |   |            |         |             |   |        |  |        |
|  | (8,576)                                   | 480        | n/m     | (25,310)    | (14,750)                                | (71.6) |  |        |
| Less: realized gains (losses) -<br>investments       | 3,803                                     | 1,120      |         | 2,402       | 3,183                                   |        |  |        |
| Less: realized gains (losses) -<br>derivatives       | 176                                       | 1,843      |         | (302)       | 2,882                                   |        |  |        |
| <b>OPERATING INCOME<br/>(LOSS)</b>                   | \$ (12,555)                               | \$ (2,483) | n/m     | \$ (27,410) | \$ (20,815)                             | (31.7) |  |        |

*For The Three Months Ended June 30, 2014 as compared to The Three Months Ended June 30, 2013**Segment operating income (loss)*

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Corporate and Other segment operating loss was \$12.6 million for the three months ended June 30, 2014, as compared to an operating loss of \$2.5 million for the three months ended June 30, 2013. The decrease was primarily due to a favorable \$3.9 million guaranty fund allocation to business segments in the second quarter of 2013 and higher overhead expenses for the second quarter of 2014. In addition, the decrease was driven by a \$2.5 million decrease in mortgage loan prepayment fee income as compared to the second quarter of 2013. These decreases were partially offset by a \$2.5 million favorable variance related to gains on the repurchase of non-recourse funding obligations as compared to the three months ended June 30, 2013.

### *Operating revenues*

Net investment income for the segment decreased \$1.5 million, or 3.3%, for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013. The decrease in net investment income was primarily due to a \$2.5 million unfavorable variance related to mortgage loan prepayment fee income partially offset by an increase of \$1.1 million related to a portfolio of securities designated for trading as compared to the three months ended June 30, 2013. Net premiums and policy fees decreased \$0.5 million, or 10.5%, for the three months ended June 30, 2014. Other income increased \$2.3 million for the three months ended June 30, 2014 as compared to the three months ended June 30, 2013, primarily due to a \$2.5 million favorable variance related to gains generated on the repurchase of non-

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recourse funding obligations. For the second quarter of 2014, \$4.6 million of pre-tax gains were generated from these repurchases compared to \$2.1 million of pre-tax gains during the second quarter of 2013.

*Total benefits and expenses*

Total benefits and expenses increased \$10.4 million for the three months ended June 30, 2014, as compared to the three months ended June 30, 2013, primarily due to a favorable \$3.9 million guaranty fund allocation to business segments in the second quarter of 2013 and higher overhead expenses for the second quarter of 2014.

***For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013***

*Segment operating income (loss)*

Corporate and Other segment operating loss was \$27.4 million for the six months ended June 30, 2014, as compared to an operating loss of \$20.8 million for the six months ended June 30, 2013. The decrease resulted from a decline in net investment income and an increase in other operating expenses as compared to the six months ended June 30, 2013. The decrease in net investment income was primarily driven by a \$2.6 million unfavorable variance related to mortgage loan prepayment fee income, an unfavorable variance related to income on called securities, and lower core investment income. The increase in other operating expenses was primarily due to higher overhead expenses for the six months ended June 30, 2014. These decreases were partially offset by a \$1.2 million favorable variance related to gains on the repurchase of non-recourse funding obligations.

*Operating revenues*

Net investment income for the segment decreased \$5.6 million, or 6.5%, for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013. The decrease in net investment income was primarily due to a \$2.6 million unfavorable variance related to mortgage loan prepayment fee income, an unfavorable variance related to income on called securities, and lower core investment income. Net premiums and policy fees decreased \$0.8 million, or 8.1%, for the six months ended June 30, 2014. Other income increased \$1.4 million for the six months ended June 30, 2014 as compared to the six months ended June 30, 2013, primarily due to a \$1.2 million favorable variance related to gains generated on the repurchase of non-recourse funding obligations. For the six months ended June 30, 2014, \$4.6 million of pre-tax gains were generated from these repurchases compared to \$3.4 million of pre-tax gains during the six months ended June 30, 2013.

*Total benefits and expenses*

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Total benefits and expenses increased \$1.6 million for the six months ended June 30, 2014, as compared to the six months ended June 30, 2013, primarily due to higher overhead expenses for the six months ended June 30, 2014.

Table of Contents**CONSOLIDATED INVESTMENTS**

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

**Portfolio Description**

As of June 30, 2014, our investment portfolio was approximately \$46.1 billion. The types of assets in which we may invest are influenced by various state insurance laws which prescribe qualified investment assets. Within the parameters of these laws, we invest in assets giving consideration to such factors as liquidity and capital needs, investment quality, investment return, matching of assets and liabilities, and the overall composition of the investment portfolio by asset type and credit exposure.

The following table presents the reported values of our invested assets:

|  | June 30, 2014 | As of                  |               | December 31, 2013 |  |
|--|---------------|------------------------|---------------|-------------------|--|
|  |               | (Dollars In Thousands) |               |                   |  |
| Publicly issued bonds (amortized cost: 2014 - \$26,773,132; 2013 - \$26,110,087) | \$ 29,161,306 | 63.2%                  | \$ 27,066,787 | 61.8%             |  |
| Privately issued bonds (amortized cost: 2014 - \$7,870,956; 2013 - \$7,917,208)  | 8,403,121     | 18.2                   | 8,114,144     | 18.5              |  |
| Fixed maturities   | 37,564,427    | 81.4                   | 35,180,931    | 80.3              |  |
| Equity securities (cost: 2014 - \$771,004; 2013 - \$675,758)                     | 792,047       | 1.7                    | 646,027       | 1.5               |  |
| Mortgage loans   | 5,294,729     | 11.5                   | 5,493,492     | 12.5              |  |
| Investment real estate   | 18,856        |                        | 20,413        |                   |  |
| Policy loans   | 1,778,379     | 3.9                    | 1,815,744     | 4.1               |  |
| Other long-term investments  | 475,719       | 1.0                    | 521,811       | 1.2               |  |
| Short-term investments   | 208,624       | 0.5                    | 134,146       | 0.4               |  |
| Total investments  | \$ 46,132,781 | 100.0%                 | \$ 43,812,564 | 100.0%            |  |

Included in the preceding table are \$2.9 billion and \$2.8 billion of fixed maturities and \$91.1 million and \$52.4 million of short-term investments classified as trading securities as of June 30, 2014 and December 31, 2013, respectively. The trading portfolio includes invested assets of \$2.9 billion and \$2.8 billion as of June 30, 2014 and December 31, 2013, respectively, held pursuant to modified coinsurance ( Modco ) arrangements under which the economic risks and benefits of the investments are passed to third party reinsurers. Also included above are \$400.0 million and \$365.0 million of securities classified as held-to-maturity as of June 30, 2014 and December 31, 2013, respectively.

**Fixed Maturity Investments**



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As of June 30, 2014, our fixed maturity investment holdings were approximately \$37.6 billion. The approximate percentage distribution of our fixed maturity investments by quality rating is as follows:

| Rating                 | As of         |                   |
|------------------------|---------------|-------------------|
|                        | June 30, 2014 | December 31, 2013 |
| AAA                    | 12.1%         | 12.5%             |
| AA                     | 7.1           | 7.0               |
| A                      | 32.5          | 32.2              |
| BBB                    | 41.6          | 41.7              |
| Below investment grade | 5.6           | 5.6               |
| Not rated              | 1.1           | 1.0               |
|                        | 100.0%        | 100.0%            |

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We use various Nationally Recognized Statistical Rating Organizations ( NRSRO ) ratings when classifying securities by quality ratings. When the various NRSRO ratings are not consistent for a security, we use the second-highest convention in assigning the rating. When there are no such published ratings, we assign a rating based on the statutory accounting rating system if such ratings are available.

We do not have material exposure to financial guarantee insurance companies with respect to our investment portfolio. As of June 30, 2014, based upon amortized cost, \$37.5 million of our securities were guaranteed either directly or indirectly by third parties out of a total of \$34.3 billion fixed maturity securities held by us (0.1% of total fixed maturity securities).

Changes in fair value for our available-for-sale portfolio, net of related DAC, VOBA, and policyholder dividend obligation are charged or credited directly to shareowners' equity, net of tax. Declines in fair value that are other-than-temporary are recorded as realized losses in the consolidated condensed statements of income, net of any applicable non-credit component of the loss, which is recorded as an adjustment to other comprehensive income (loss).

The distribution of our fixed maturity investments by type is as follows:

| Type   | As of                 |                   |
|--|-----------------------|-------------------|
|  | June 30, 2014         | December 31, 2013 |
|  | (Dollars In Millions) |                   |
| Corporate bonds                                | \$ 29,297.3           | \$ 27,286.2       |
| Residential mortgage-backed securities         | 1,734.2               | 1,756.0           |
| Commercial mortgage-backed securities          | 1,247.5               | 1,129.2           |
| Other asset-backed securities                  | 1,137.1               | 1,160.2           |
| U.S. government-related securities             | 1,785.9               | 1,704.1           |
| Other government-related securities            | 78.4                  | 108.5             |
| States, municipals, and political subdivisions | 1,884.0               | 1,671.7           |
| Other  | 400.0                 | 365.0             |
| Total fixed income portfolio                   | \$ 37,564.4           | \$ 35,180.9       |

Within our fixed maturity investments, we maintain portfolios classified as available-for-sale, trading, and held-to-maturity. We purchase our available-for-sale investments with the intent to hold to maturity by purchasing investments that match future cash flow needs. However, we may sell any of our available-for-sale and trading investments to maintain proper matching of assets and liabilities. Accordingly, we classified \$34.3 billion, or 91.3%, of our fixed maturities as available-for-sale as of June 30, 2014. These securities are carried at fair value on our consolidated condensed balance sheets.

Fixed maturities that we have both the positive intent and ability to hold to maturity are classified as held-to-maturity. We classified \$400.0 million, or 1.1% of our fixed maturities as held-to-maturity as of June 30, 2014. These securities are carried at amortized cost on our consolidated condensed balance sheets.

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Trading securities are carried at fair value and changes in fair value are recorded on the income statement as they occur. Our trading portfolio accounts for \$2.9 billion, or 7.6%, of our fixed maturities and \$91.1 million of short-term investments as of June 30, 2014. Changes in fair value on the trading portfolio, including gains and losses from sales, are passed to the reinsurers through the contractual terms of the reinsurance arrangements. Partially offsetting these amounts are corresponding changes in the fair value of the embedded derivative associated with the underlying reinsurance arrangement. The total Modco trading portfolio fixed maturities by rating is as follows:

| Rating                               | As of                  |                   |
|--------------------------------------|------------------------|-------------------|
|                                      | June 30, 2014          | December 31, 2013 |
|                                      | (Dollars In Thousands) |                   |
| AAA                                  | \$ 428,959             | \$ 419,866        |
| AA                                   | 278,151                | 266,173           |
| A                                    | 870,292                | 854,020           |
| BBB                                  | 942,742                | 924,554           |
| Below investment grade               | 330,833                | 324,453           |
| Total Modco trading fixed maturities | \$ 2,850,977           | \$ 2,789,066      |

A portion of our bond portfolio is invested in residential mortgage-backed securities ( RMBS ), commercial mortgage-backed securities ( CMBS ), and other asset-backed securities (collectively referred to as asset-backed securities or ABS ). ABS are securities that are backed by a pool of assets. These holdings as of June 30, 2014, were approximately \$4.1 billion. Mortgage-backed securities ( MBS ) are constructed from pools of mortgages and may have cash flow volatility as a result of changes in the rate at which prepayments of principal occur with respect to the underlying loans. Excluding limitations on access to lending and other extraordinary economic conditions, prepayments of principal on the underlying loans can be expected to accelerate with decreases in market interest rates and diminish with increases in interest rates.

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**Residential mortgage-backed securities** - As of June 30, 2014, our RMBS portfolio was approximately \$1.7 billion. Sequential securities receive payments in order until each class is paid off. Planned amortization class securities ( PACs ) pay down according to a schedule. Pass through securities receive principal as principal of the underlying mortgages is received.

The tables below include a breakdown of these holdings by type and rating as of June 30, 2014.

| Type         | Percentage of<br>Residential<br>Mortgage-<br>Backed<br>Securities |
|--------------|---|
| Sequential   | 25.6%   |
| PAC          | 37.7  |
| Pass Through | 10.8  |
| Other        | 25.9  |
|              | 100.0%  |

| Rating                 | Percentage of<br>Residential<br>Mortgage-Backed<br>Securities |
|------------------------|---|
| AAA                    | 62.3%   |
| AA                     | 0.2   |
| A                      | 0.9   |
| BBB                    | 0.4   |
| Below investment grade | 36.2  |
|                        | 100.0%  |

Table of Contents*Alt-A Collateralized Holdings*

As of June 30, 2014, we held securities with a fair value of \$388.4 million, or 0.8% of invested assets, supported by collateral classified as Alt-A. As of December 31, 2013, we held securities with a fair value of \$395.0 million supported by collateral classified as Alt-A. We included in this classification certain whole loan securities where such securities had underlying mortgages with a high level of limited loan documentation. As of June 30, 2014, these securities had a fair value of \$140.5 million and an unrealized gain of \$34.5 million.

The following table includes the percentage of our collateral classified as Alt-A, grouped by rating category, as of June 30, 2014:

| Rating                 | Percentage of<br>Alt-A<br>Securities |
|------------------------|--------------------------------------|
| A                      | 1.3%                                 |
| BBB                    | 0.3                                  |
| Below investment grade | 98.4                                 |
|                        | 100.0%                               |

The following tables categorize the estimated fair value and unrealized gain/(loss) of our mortgage-backed securities collateralized by Alt-A mortgage loans by rating as of June 30, 2014:

**Alt-A Collateralized Holdings**

| Rating   | Estimated Fair Value of Security by Year of Security Origination |      |      |      |      |          |
|--|--|------|------|------|------|----------|
|  | 2010 and<br>Prior  | 2011 | 2012 | 2013 | 2014 | Total    |
|  | (Dollars In Millions)  |      |      |      |      |          |
| A  | \$ 5.0   | \$   | \$   | \$   | \$   | \$ 5.0   |
| BBB  | 1.3  |      |      |      |      | 1.3      |
| Below investment grade   | 382.1  |      |      |      |      | 382.1    |
| Total mortgage-backed securities collateralized<br>by Alt-A mortgage loans | \$ 388.4   | \$   | \$   | \$   | \$   | \$ 388.4 |

| Rating   | Estimated Unrealized Gain (Loss) of Security by Year of Security Origination |      |      |      |      |         |
|--|--|------|------|------|------|---------|
|  | 2010 and<br>Prior  | 2011 | 2012 | 2013 | 2014 | Total   |
|  | (Dollars In Millions)  |      |      |      |      |         |
| A  | \$ 0.2   | \$   | \$   | \$   | \$   | \$ 0.2  |
| BBB  | 0.1  |      |      |      |      | 0.1     |
| Below investment grade   | 42.8   |      |      |      |      | 42.8    |
| Total mortgage-backed securities collateralized<br>by Alt-A mortgage loans | \$ 43.1  | \$   | \$   | \$   | \$   | \$ 43.1 |



Table of Contents***Sub-prime Collateralized Holdings***

As of June 30, 2014, we held securities with a total fair value of \$1.9 million that were supported by collateral classified as sub-prime. As of December 31, 2013, we held securities with a fair value of \$2.0 million that were supported by collateral classified as sub-prime.

***Prime Collateralized Holdings***

As of June 30, 2014, we had RMBS collateralized by prime mortgage loans (including agency mortgages) with a total fair value of \$1.3 billion, or 2.9%, of total invested assets. As of December 31, 2013, we held securities with a fair value of \$1.4 billion of RMBS collateralized by prime mortgage loans (including agency mortgages).

The following table includes the percentage of our collateral classified as prime, grouped by rating category, as of June 30, 2014:

| Rating                 | Percentage of Prime Securities |
|------------------------|--------------------------------|
| AAA                    | 80.4%                          |
| AA                     | 0.2                            |
| A                      | 0.8                            |
| BBB                    | 0.5                            |
| Below investment grade | 18.1                           |
|                        | 100.0%                         |

The following tables categorize the estimated fair value and unrealized gain/(loss) of our mortgage-backed securities collateralized by prime mortgage loans (including agency mortgages) by rating as of June 30, 2014:

**Prime Collateralized Holdings**

| Rating  | Estimated Fair Value of Security by Year of Security Origination |          |         |          |         | Total      |
|---|--|----------|---------|----------|---------|------------|
|   | 2010 and Prior   | 2011     | 2012    | 2013     | 2014    |            |
|   | (Dollars In Millions)  |          |         |          |         |            |
| AAA   | \$ 532.5   | \$ 317.7 | \$ 27.2 | \$ 140.9 | \$ 62.5 | \$ 1,080.8 |
| AA  | 0.2  |          |         |          | 2.6     | 2.8        |
| A   | 11.0   |          |         |          |         | 11.0       |
| BBB   | 6.4  |          |         |          |         | 6.4        |
| Below investment grade  | 242.9  |          |         |          |         | 242.9      |
| Total mortgage-backed securities collateralized by prime mortgage loans | \$ 793.0   | \$ 317.7 | \$ 27.2 | \$ 140.9 | \$ 65.1 | \$ 1,343.9 |

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| Rating   | Estimated Unrealized Gain (Loss) of Security by Year of Security Origination |         |        |        |          |                       | Total |
|--|--|---------|--------|--------|----------|-----------------------|-------|
|  | 2010 and<br>Prior  | 2011    | 2012   | 2013   | 2014     | (Dollars In Millions) |       |
| AAA  | \$ 26.3  | \$ 12.1 | \$ 0.1 | \$ 0.5 | \$ (1.7) | \$ 37.3               |       |
| AA   |  |         |        |        |          |                       |       |
| A  | 0.8  |         |        |        |          | 0.8                   |       |
| BBB  | 0.5  |         |        |        |          | 0.5                   |       |
| Below investment grade   | 10.9   |         |        |        |          | 10.9                  |       |
| Total mortgage-backed securities<br>collateralized by prime mortgage loans | \$ 38.5  | \$ 12.1 | \$ 0.1 | \$ 0.5 | \$ (1.7) | \$ 49.5               |       |



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**Commercial mortgage-backed securities** - Our CMBS portfolio consists of commercial mortgage-backed securities issued in securitization transactions. As of June 30, 2014, the CMBS holdings were approximately \$1.2 billion. As of December 31, 2013, the CMBS holdings were approximately \$1.1 billion.

The following table includes the percentages of our CMBS holdings, grouped by rating category, as of June 30, 2014:

| Rating | Percentage of Commercial Mortgage-Backed Securities |
|--------|---|
| AAA    | 70.6%   |
| AA     | 14.2  |
| A      | 12.5  |
| BBB    | 2.7   |
|        | 100.0%  |

The following tables categorize the estimated fair value and unrealized gain/(loss) of our CMBS as of June 30, 2014:

**Commercial Mortgage-Backed Securities**

| Rating                                      | Estimated Fair Value of Security by Year of Security Origination |          |          |          |         |                       | Total |
|---|--|----------|----------|----------|---------|-----------------------|-------|
|   | 2010 and Prior   | 2011     | 2012     | 2013     | 2014    | (Dollars In Millions) |       |
| AAA   | \$ 151.0   | \$ 214.8 | \$ 310.9 | \$ 149.1 | \$ 54.6 | \$ 880.4              |       |
| AA  | 42.1   | 38.7     | 43.0     | 30.2     | 23.0    | 177.0                 |       |
| A   | 70.8   | 52.5     | 13.5     | 19.7     |         | 156.5                 |       |
| BBB   | 33.6   |          |          |          |         | 33.6                  |       |
| Total commercial mortgage-backed securities | \$ 297.5   | \$ 306.0 | \$ 367.4 | \$ 199.0 | \$ 77.6 | \$ 1,247.5            |       |

| Rating                                      | Estimated Unrealized Gain (Loss) of Security by Year of Security Origination |         |        |        |        |                       | Total |
|---|--|---------|--------|--------|--------|-----------------------|-------|
|   | 2010 and Prior   | 2011    | 2012   | 2013   | 2014   | (Dollars In Millions) |       |
| AAA   | \$ 9.4   | \$ 21.8 | \$ 5.7 | \$ 1.7 | \$ 1.0 | \$ 39.6               |       |
| AA  | 2.6  | 3.7     | (1.0)  |        | 0.5    | 5.8                   |       |
| A   | 3.2  | 1.0     | (0.8)  | (0.8)  |        | 2.6                   |       |
| BBB   | 0.6  |         |        |        |        | 0.6                   |       |
| Total commercial mortgage-backed securities | \$ 15.8  | \$ 26.5 | \$ 3.9 | \$ 0.9 | \$ 1.5 | \$ 48.6               |       |

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**Other asset-backed securities** Other asset-backed securities pay down based on cash flow received from the underlying pool of assets, such as receivables on auto loans, student loans, credit cards, etc. As of June 30, 2014, these holdings were approximately \$1.1 billion. As of December 31, 2013, these holdings were approximately \$1.2 billion.

The following table includes the percentages of our other asset-backed holdings, grouped by rating category, as of June 30, 2014:

| Rating                 | Percentage of Other Asset-Backed Securities |
|------------------------|---|
| AAA                    | 49.6%                                       |
| AA                     | 19.6  |
| A                      | 17.7  |
| BBB                    | 0.6   |
| Below investment grade | 12.5  |
|                        | 100.0%                                      |

The following tables categorize the estimated fair value and unrealized gain/(loss) of our asset-backed securities as of June 30, 2014:

**Other Asset-Backed Securities**

| Rating                              | Estimated Fair Value of Security by Year of Security Origination |         |          |         |         |                       | Total   |
|-------------------------------------|--|---------|----------|---------|---------|-----------------------|---------|
|                                     | 2010 and Prior   | 2011    | 2012     | 2013    | 2014    | (Dollars In Millions) |         |
| AAA                                 | \$ 490.3   | \$ 13.5 | \$ 32.6  | \$ 19.3 | \$ 8.3  | \$                    | 564.0   |
| AA                                  | 159.4  |         | 63.5     |         |         |                       | 222.9   |
| A                                   | 43.6   | 52.0    | 62.2     | 33.5    | 10.1    |                       | 201.4   |
| BBB                                 | 6.4  |         |          |         |         |                       | 6.4     |
| Below investment grade              | 142.4  |         |          |         |         |                       | 142.4   |
| Total other asset-backed securities | \$ 842.1   | \$ 65.5 | \$ 158.3 | \$ 52.8 | \$ 18.4 | \$                    | 1,137.1 |

| Rating                              | Estimated Unrealized Gain (Loss) of Security by Year of Security Origination |        |        |        |        |                       | Total  |
|-------------------------------------|--|--------|--------|--------|--------|-----------------------|--------|
|                                     | 2010 and Prior   | 2011   | 2012   | 2013   | 2014   | (Dollars In Millions) |        |
| AAA                                 | \$ (15.3)  | \$ 1.2 | \$ 0.6 | \$ 0.6 | \$ 0.2 | \$                    | (12.7) |
| AA                                  | (8.9)  |        | (0.3)  |        |        |                       | (9.2)  |
| A                                   | 4.0  | 4.8    | (0.2)  | 0.3    | 0.1    |                       | 9.0    |
| BBB                                 | 0.3  |        |        |        |        |                       | 0.3    |
| Below investment grade              | 18.0   |        |        |        |        |                       | 18.0   |
| Total other asset-backed securities | \$ (1.9)   | \$ 6.0 | \$ 0.1 | \$ 0.9 | \$ 0.3 | \$                    | 5.4    |

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We obtained ratings of our fixed maturities from Moody's Investors Service, Inc. ( Moody's ), Standard & Poor's Corporation ( S&P ), and/or Fitch Ratings ( Fitch ). If a fixed maturity is not rated by Moody's, S&P, or Fitch, we use ratings from the National Association of Insurance Commissioners ( NAIC ), or we rate the fixed maturity based upon a comparison of the unrated issue to rated issues of the same issuer or rated issues of other issuers with similar risk characteristics. As of June 30, 2014, 98.9% of our fixed maturities were rated by Moody's, S&P, Fitch, and/or the NAIC.

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The industry segment composition of our fixed maturity securities is presented in the following table:

|   | As of<br>June 30, 2014 | % Fair<br>Value<br>(Dollars In Thousands) | As of<br>December 31, 2013 | % Fair<br>Value |
|---|------------------------|---|----------------------------|-----------------|
| Banking   | \$ 2,884,177           | 7.7%                                      | \$ 2,664,495               | 7.6%            |
| Other finance                                     | 676,745                | 1.8                                       | 620,544                    | 1.8             |
| Electric  | 4,033,847              | 10.7                                      | 3,749,786                  | 10.7            |
| Natural gas                                       | 2,719,136              | 7.2                                       | 2,369,185                  | 6.7             |
| Insurance   | 2,871,695              | 7.6                                       | 2,634,325                  | 7.5             |
| Energy  | 2,090,766              | 5.6                                       | 1,947,154                  | 5.5             |
| Communications                                    | 1,568,921              | 4.2                                       | 1,500,544                  | 4.3             |
| Basic industrial                                  | 1,851,600              | 4.9                                       | 1,674,169                  | 4.8             |
| Consumer noncyclical                              | 3,226,197              | 8.6                                       | 3,040,080                  | 8.6             |
| Consumer cyclical                                 | 2,144,313              | 5.7                                       | 2,141,961                  | 6.1             |
| Finance companies                                 | 249,730                | 0.7                                       | 261,871                    | 0.7             |
| Capital goods                                     | 1,388,775              | 3.7                                       | 1,300,671                  | 3.7             |
| Transportation                                    | 947,066                | 2.5                                       | 909,574                    | 2.6             |
| Other industrial                                  | 362,104                | 1.0                                       | 386,079                    | 1.1             |
| Brokerage   | 653,888                | 1.7                                       | 627,630                    | 1.8             |
| Technology  | 1,121,045              | 3.0                                       | 1,009,357                  | 2.9             |
| Real estate                                       | 274,974                | 0.7                                       | 269,378                    | 0.8             |
| Other utility                                     | 232,357                | 0.6                                       | 179,346                    | 0.5             |
| Commercial mortgage-backed securities             | 1,247,513              | 3.3                                       | 1,129,226                  | 3.2             |
| Other asset-backed securities                     | 1,137,083              | 3.0                                       | 1,160,238                  | 3.3             |
| Residential mortgage-backed non-agency securities | 783,302                | 2.1                                       | 800,154                    | 2.3             |
| Residential mortgage-backed agency securities     | 950,961                | 2.5                                       | 955,791                    | 2.7             |
| U.S. government-related securities                | 1,785,846              | 4.8                                       | 1,704,128                  | 4.8             |
| Other government-related securities               | 78,355                 | 0.2                                       | 108,524                    | 0.3             |
| State, municipals, and political divisions        | 1,884,031              | 5.0                                       | 1,671,721                  | 4.8             |
| Other   | 400,000                | 1.2                                       | 365,000                    | 0.9             |
| <b>Total</b>                                      | <b>\$ 37,564,427</b>   | <b>100.0%</b>                             | <b>\$ 35,180,931</b>       | <b>100.0%</b>   |

Our investments classified as available-for-sale and trading in debt and equity securities are reported at fair value. Our investments classified as held-to-maturity are reported at amortized cost. As of June 30, 2014, our fixed maturity investments (bonds and redeemable preferred stocks) had a market value of \$37.6 billion, which was 9.6% above amortized cost of \$34.3 billion. These assets are invested for terms approximately corresponding to anticipated future benefit payments. Thus, market fluctuations are not expected to adversely affect liquidity.

Market values for private, non-traded securities are determined as follows: 1) we obtain estimates from independent pricing services and 2) we estimate market value based upon a comparison to quoted issues of the same issuer or issues of other issuers with similar terms and risk characteristics. We analyze the independent pricing services valuation methodologies and related inputs, including an assessment of the observability of market inputs. Upon obtaining this information related to market value, management makes a determination as to the appropriate valuation amount.

### **Mortgage Loans**

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We invest a portion of our investment portfolio in commercial mortgage loans. As of June 30, 2014, our mortgage loan holdings were approximately \$5.3 billion. We have specialized in making loans on either credit-oriented commercial properties or credit-anchored strip shopping centers and apartments. Our underwriting procedures relative to our commercial loan portfolio are based, in our view, on a conservative and disciplined approach. We concentrate on a small number of commercial real estate asset types associated with the necessities of life (retail, multi-family, professional office buildings, and warehouses). We believe these asset types tend to weather economic downturns better

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than other commercial asset classes in which it has chosen not to participate. We believe this disciplined approach has helped to maintain a relatively low delinquency and foreclosure rate throughout its history. The majority of our mortgage loans portfolio was underwritten and funded by us. From time to time, we may acquire loans in conjunction with an acquisition.

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

Certain of our mortgage loans have call options or interest rate reset options between 3 and 10 years. However, if interest rates were to significantly increase, we may be unable to exercise the call options or increase the interest rates on our existing mortgage loans commensurate with the significantly increased market rates. Assuming the loans are called at their next call dates, approximately \$43.7 million would become due for the remainder of 2014, \$1.1 billion in 2015 through 2019, \$501.4 million in 2020 through 2024, and \$130.5 million thereafter.

We also offer a type of commercial mortgage loan under which we will permit a loan-to-value ratio of up to 85% in exchange for a participating interest in the cash flows from the underlying real estate. As of June 30, 2014 and December 31, 2013, approximately \$613.8 million and \$666.6 million, respectively, of our mortgage loans had this participation feature. Cash flows received as a result of this participation feature are recorded as interest income. During the three and six month period ended June 30, 2014 and 2013, we recognized \$2.8 million and \$5.8 million and \$5.8 million and \$9.2 million, respectively, of participating mortgage loan income.

We record mortgage loans net of an allowance for credit losses. This allowance is calculated through analysis of specific loans that have indicators of potential impairment based on current information and events. As of June 30, 2014 and December 31, 2013, our allowance for mortgage loan credit losses was \$4.3 million and \$3.1 million, respectively. While our mortgage loans do not have quoted market values, as of June 30, 2014, we estimated the fair value of our mortgage loans to be \$5.8 billion (using discounted cash flows from the next call date), which was approximately 9.3% greater than the amortized cost, less any related loan loss reserve.

At the time of origination, our mortgage lending criteria targets that the loan-to-value ratio on each mortgage is 75% or less. We target projected rental payments from credit anchors (i.e., excluding rental payments from smaller local tenants) of 70% of the property's projected operating expenses and debt service.

As of June 30, 2014, approximately \$5.9 million, or 0.01%, of invested assets consisted of nonperforming, restructured or mortgage loans that were foreclosed and were converted to real estate properties. We do not expect these investments to adversely affect its liquidity or ability to maintain proper matching of assets and liabilities. During the six months ended June 30, 2014, certain mortgage loan transactions occurred that were accounted for as troubled debt restructurings under Topic 310 of the FASB ASC. For all mortgage loans, the impact of troubled debt restructurings is generally reflected in our investment balance and in the allowance for mortgage loan credit losses. Transactions accounted for as troubled debt restructurings during the quarter included acceptance of assets in satisfaction of principal, and were the result of agreements between the creditor and the debtor. During the three and six month periods ending June 30, 2014, we accepted assets of \$15.1 million in satisfaction of \$16.0 million of principal resulting in a \$0.9 million decrease in our investment in mortgage loans net of existing allowances for mortgage loan losses. No loans classified as troubled debt restructurings remained on our balance sheet as of June 30, 2014.

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Our mortgage loan portfolio consists of two categories of loans: (1) those not subject to a pooling and servicing agreement and (2) those subject to a contractual pooling and servicing agreement. As of June 30, 2014, \$3.7 million of mortgage loans not subject to a pooling and servicing agreement were nonperforming or restructured. None of these nonperforming loans have been restructured during the six months ended June 30, 2014. We did not foreclose on any loans during the six months ended June 30, 2014.

As of June 30, 2014, \$2.2 million of loans subject to a pooling and servicing agreement were nonperforming. None of these nonperforming loans have been restructured during the six months ended June 30, 2014. We did not foreclose on any loans during the six months ended June 30, 2014.

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We do not expect these investments to adversely affect our liquidity or ability to maintain proper matching of assets and liabilities.

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

**Risk Management and Impairment Review**

We monitor the overall credit quality of our portfolio within established guidelines. The following table includes our available-for-sale fixed maturities by credit rating as of June 30, 2014:

| Rating                 | Fair Value<br>(Dollars In Thousands) | Percent of<br>Fair Value |
|------------------------|--------------------------------------|--------------------------|
| AAA                    | \$ 4,125,799                         | 12.0%                    |
| AA                     | 2,406,877                            | 7.0                      |
| A                      | 11,327,322                           | 33.0                     |
| BBB                    | 14,701,968                           | 42.9                     |
| Investment grade       | 32,561,966                           | 94.9                     |
| BB                     | 1,113,236                            | 3.2                      |
| B                      | 144,850                              | 0.4                      |
| CCC or lower           | 489,686                              | 1.5                      |
| Below investment grade | 1,747,772                            | 5.1                      |
| Total                  | \$ 34,309,738                        | 100.0%                   |

Not included in the table above are \$2.5 billion of investment grade and \$334.5 million of below investment grade fixed maturities classified as trading securities and \$400.0 million of fixed maturities classified as held-to-maturity.

Limiting bond exposure to any creditor group is another way we manage credit risk. We held no credit default swaps on the positions listed below as of June 30, 2014. The following table summarizes our ten largest maturity exposures to an individual creditor group as of June 30, 2014:

| Creditor                | Fair Value of         |                       | Total<br>Fair Value |
|-------------------------|-----------------------|-----------------------|---------------------|
|                         | Funded<br>Securities  | Unfunded<br>Exposures |                     |
|                         | (Dollars In Millions) |                       |                     |
| Berkshire Hathaway Inc. | \$ 227.3              | \$                    | \$ 227.3            |
| Duke Energy Corp.       | 199.3                 |                       | 199.3               |
| Bank of America Corp.   | 192.5                 | 1.0                   | 193.5               |



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|                             |       |      |       |
|-----------------------------|-------|------|-------|
| General Electric            | 191.7 |      | 191.7 |
| Comcast Corp.               | 190.4 |      | 190.4 |
| AT&T Inc.                   | 183.0 |      | 183.0 |
| Wells Fargo & Co.           | 182.8 | 1.2  | 184.0 |
| JP Morgan Chase and Company | 157.5 | 17.5 | 175.0 |
| Nextera Energy Inc.         | 174.2 |      | 174.2 |
| Exelon Corp.                | 173.1 |      | 173.1 |

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Determining whether a decline in the current fair value of invested assets is an other-than-temporary decline in value is both objective and subjective, and can involve a variety of assumptions and estimates, particularly for investments that are not actively traded in established markets. We review our positions on a monthly basis for possible credit concerns and review our current exposure, credit enhancement, and delinquency experience.

Management considers a number of factors when determining the impairment status of individual securities. These include the economic condition of various industry segments and geographic locations and other areas of identified risks. Since it is possible for the impairment of one investment to affect other investments, we engage in ongoing risk management to safeguard against and limit any further risk to our investment portfolio. Special attention is given to correlative risks within specific industries, related parties, and business markets.

For certain securitized financial assets with contractual cash flows, including RMBS, CMBS, and other asset-backed securities (collectively referred to as asset-backed securities or ABS), GAAP requires us to periodically update our best estimate of cash flows over the life of the security. If the fair value of a securitized financial asset is less than its cost or amortized cost and there has been a decrease in the present value of the expected cash flows since the last revised estimate, considering both timing and amount, an other-than-temporary impairment charge is recognized. Estimating future cash flows is a quantitative and qualitative process that incorporates information received from third party sources along with certain internal assumptions and judgments regarding the future performance of the underlying collateral. Projections of expected future cash flows may change based upon new information regarding the performance of the underlying collateral. In addition, we consider our intent and ability to retain a temporarily depressed security until recovery.

Securities in an unrealized loss position are reviewed at least quarterly to determine if an other-than-temporary impairment is present based on certain quantitative and qualitative factors. We consider a number of factors in determining whether the impairment is other-than-temporary. 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 our intent to sell the security (including a more likely than not assessment of whether we will be required to sell the security) before recovering the security's amortized cost, 5) the duration of the decline, 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, along with an analysis regarding our expectations for recovery of the security's entire amortized cost basis through the receipt of future cash flows. Based on our analysis, for the three and six months ended June 30, 2014, we concluded that approximately \$1.5 million and \$3.1 million, respectively, of investment securities in an unrealized loss position was other-than-temporarily impaired, due to credit-related factors, resulting in a charge to earnings. Additionally, we recognized \$1.0 million and \$2.2 million, respectively, of non-credit losses previously recorded in other comprehensive income (loss) that were recorded in earnings. These non-credit gains were caused by recognizing, in the current quarter, credit losses in earnings that had previously been recognized as non-credit losses in other comprehensive income.

There are certain risks and uncertainties associated with determining whether declines in market values are other-than-temporary. These include significant changes in general economic conditions and business markets, trends in certain industry segments, interest rate fluctuations, rating agency actions, changes in significant accounting estimates and assumptions, commission of fraud, and legislative actions. We continuously monitor these factors as they relate to the investment portfolio in determining the status of each investment.

We have deposits with certain financial institutions which exceed federally insured limits. We have reviewed the creditworthiness of these financial institutions and believe there is minimal risk of a material loss.

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Certain European countries have experienced varying degrees of financial stress. Risks from the continued debt crisis in Europe could continue to disrupt the financial markets which could have a detrimental impact on global economic conditions and on sovereign and non-sovereign obligations. There remains considerable uncertainty as to future developments in the European debt crisis and the impact on financial markets.

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The chart shown below includes our non-sovereign fair value exposures in these countries as of June 30, 2014. As June 30, 2014, we had no unfunded exposure and had no direct sovereign fair value exposure.

| Financial Instrument and Country | Non-sovereign Debt |  | Total Gross<br>Funded<br>Exposure |
|----------------------------------|--------------------|--|-----------------------------------|
|                                  | Financial          | Non-financial<br>(Dollars In Millions) |                                   |
| <b>Securities:</b>               |                    |  |                                   |
| United Kingdom                   | \$ 628.2           | \$ 734.1                               | \$ 1,362.3                        |
| Netherlands                      | 160.5              | 223.4                                  | 383.9                             |
| France                           | 117.3              | 239.1                                  | 356.4                             |
| Switzerland                      | 152.2              | 162.4                                  | 314.6                             |
| Germany                          | 109.1              | 134.2                                  | 243.3                             |
| Spain                            | 43.2               | 148.7                                  | 191.9                             |
| Sweden                           | 122.2              | 38.3                                   | 160.5                             |
| Belgium                          |                    | 111.6                                  | 111.6                             |
| Italy                            |                    | 108.3                                  | 108.3                             |
| Norway                           | 12.5               | 91.0                                   | 103.5                             |
| Ireland                          | 11.5               | 69.5                                   | 81.0                              |
| Luxembourg                       |                    | 73.6                                   | 73.6                              |
| Total securities                 | 1,356.7            | 2,134.2                                | 3,490.9                           |
| <b>Derivatives:</b>              |                    |  |                                   |
| United Kingdom                   | 13.5               |  | 13.5                              |
| Switzerland                      | 8.7                |  | 8.7                               |
| Germany                          | 7.8                |  | 7.8                               |
| Total derivatives                | 30.0               |  | 30.0                              |
| Total securities                 | \$ 1,386.7         | \$ 2,134.2                             | \$ 3,520.9                        |

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The following table sets forth realized investment gains and losses for the periods shown:

|   | For The<br>Three Months Ended<br>June 30, |              |                                  | For The<br>Six Months Ended<br>June 30, |              |              | Change |
|---|---|--------------|----------------------------------|---|--------------|--------------|--------|
|   | 2014                                      | 2013         | Change<br>(Dollars In Thousands) | 2014                                    | 2013         | Change       |        |
| Fixed maturity gains - sales                            | \$ 20,437                                 | \$ 21,579    | \$ (1,142)                       | \$ 28,064                               | \$ 34,444    | \$ (6,380)   |        |
| Fixed maturity losses - sales                           | (239)                                     | (2,427)      | 2,188                            | (496)                                   | (2,983)      | 2,487        |        |
| Equity gains - sales                                    |   | 2,366        | (2,366)                          |   | 2,367        | (2,367)      |        |
| Impairments on fixed maturity securities                | (1,460)                                   | (2,910)      | 1,450                            | (3,051)                                 | (6,497)      | 3,446        |        |
| Impairments on equity securities                        |   | (1,090)      | 1,090                            |   | (2,087)      | 2,087        |        |
| Modco trading portfolio                                 | 60,989                                    | (126,694)    | 187,683                          | 127,292                                 | (142,022)    | 269,314      |        |
| Other   | (1,039)                                   | (4,802)      | 3,763                            | (2,598)                                 | (5,929)      | 3,331        |        |
| Total realized gains (losses) - investments             | \$ 78,688                                 | \$ (113,978) | \$ 192,666                       | \$ 149,211                              | \$ (122,707) | \$ 271,918   |        |
| Derivatives related to variable annuity contracts:      |   |              |                                  |   |              |              |        |
| Interest rate futures - VA                              | \$ 6,548                                  | \$ (7,654)   | \$ 14,202                        | \$ 10,798                               | \$ (24,138)  | \$ 34,936    |        |
| Equity futures - VA                                     | (7,259)                                   | (4,036)      | (3,223)                          | (9,910)                                 | (27,261)     | 17,351       |        |
| Currency futures - VA                                   | (2,887)                                   | (112)        | (2,775)                          | (4,165)                                 | 7,971        | (12,136)     |        |
| Variance swaps - VA                                     | (823)                                     | 2,214        | (3,037)                          | (2,673)                                 | (8,219)      | 5,546        |        |
| Equity options - VA                                     | (20,949)                                  | (8,131)      | (12,818)                         | (33,290)                                | (36,537)     | 3,247        |        |
| Interest rate swaptions - VA                            | (4,998)                                   | 1,639        | (6,637)                          | (14,401)                                | (2,463)      | (11,938)     |        |
| Interest rate swaps - VA                                | 45,169                                    | (89,722)     | 134,891                          | 102,537                                 | (106,278)    | 208,815      |        |
| Embedded derivative - GMWB                              | (47,389)                                  | 103,315      | (150,704)                        | (129,676)                               | 183,690      | (313,366)    |        |
| Total derivatives related to variable annuity contracts | (32,588)                                  | (2,487)      | (30,101)                         | (80,780)                                | (13,235)     | (67,545)     |        |
| Derivatives related to FIA contracts:                   |   |              |                                  |   |              |              |        |
| Embedded derivative - FIA                               | (8,307)                                   | (41)         | (8,266)                          | (6,574)                                 | (41)         | (6,533)      |        |
| Equity futures - FIA                                    | 605                                       |              | 605                              | 950                                     |              | 950          |        |
| Volatility futures - FIA                                | 8   |              | 8                                | 8                                       |              | 8            |        |
| Equity options - FIA                                    | 2,984                                     | (19)         | 3,003                            | 3,978                                   | (19)         | 3,997        |        |
| Total derivatives related to FIA contracts              | (4,710)                                   | (60)         | (4,650)                          | (1,638)                                 | (60)         | (1,578)      |        |
| Embedded derivative - IUL                               | (285)                                     |              | (285)                            | (285)                                   |              | (285)        |        |
| Embedded derivative - Modco reinsurance treaties        | (52,202)                                  | 144,998      | (197,200)                        | (112,371)                               | 161,773      | (274,144)    |        |
| Interest rate swaps                                     |   | 1,909        | (1,909)                          |   | 2,912        | (2,912)      |        |
| Other derivatives                                       | (141)                                     | (479)        | 338                              | (202)                                   | (124)        | (78)         |        |
| Total realized gains (losses) - derivatives             | \$ (89,926)                               | \$ 143,881   | \$ (233,807)                     | \$ (195,276)                            | \$ 151,266   | \$ (346,542) |        |

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Realized gains and losses on investments reflect portfolio management activities designed to maintain proper matching of assets and liabilities and to enhance long-term investment portfolio performance. The change in net realized investment gains (losses), excluding impairments and Modco trading portfolio activity during the six months ended June 30, 2014, primarily reflects the normal operation of our asset/liability program within the context of the changing interest rate and spread environment, as well as tax planning strategies designed to utilize capital loss carryforwards.

Realized losses are comprised of both write-downs of other-than-temporary impairments and actual sales of investments. For the three and six months ended June 30, 2014, we recognized pre-tax other-than-temporary impairments of \$1.5 million and \$3.1 million, respectively, due to credit-related factors, resulting in a charge to earnings. Additionally, we recognized \$1.0 million and \$2.2 million, respectively, of non-credit losses previously recorded in other comprehensive income in earnings as credit losses. For the three and six months ended June 30, 2013, we recognized pre-tax other-than-temporary impairments of \$4.0 million and \$8.6 million, respectively. These other-than-temporary impairments resulted from our analysis of circumstances and our belief that credit events, loss severity, changes in credit enhancement, and/or other adverse conditions of the respective issuers have caused, or will lead to, a

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deficiency in the contractual cash flows related to these investments. These other-than-temporary impairments, net of Modco recoveries, are presented in the chart below:

|                 | For The<br>Three Months Ended<br>June 30, |        | For The<br>Six Months Ended<br>June 30, |        |
|-----------------|---|--------|---|--------|
|                 | 2014                                      | 2013   | 2014                                    | 2013   |
|                 | (Dollars In Millions)                     |        |   |        |
| Alt-A MBS       | \$ 1.0                                    | \$ 1.4 | \$ 2.0                                  | \$ 3.0 |
| Other MBS       | 0.5                                       | 1.5    | 1.1                                     | 3.5    |
| Corporate bonds |   |        |   |        |
| Sub-prime bonds |   |        |   |        |
| Equities        |   | 1.1    |   | 2.1    |
| Total           | \$ 1.5                                    | \$ 4.0 | \$ 3.1                                  | \$ 8.6 |

As previously discussed, management considers several factors when determining other-than-temporary impairments. Although we purchase securities with the intent to hold them until maturity, we may change our position as a result of a change in circumstances. Any such decision is consistent with our classification of all but a specific portion of our investment portfolio as available-for-sale. For the six months ended June 30, 2014, we sold securities in an unrealized loss position with a fair value of \$4.4 million. For such securities, the proceeds, realized loss, and total time period that the security had been in an unrealized loss position are presented in the table below:

|                           | Proceeds               | % Proceeds | Realized Loss | % Realized Loss |
|---------------------------|------------------------|------------|---------------|-----------------|
|                           | (Dollars In Thousands) |            |               |                 |
| <= 90 days                | \$ 2,544               | 58.0%      | \$ (197)      | 39.6%           |
| >90 days but <= 180 days  | 193                    | 4.4        | (2)           | 0.5             |
| >180 days but <= 270 days | 209                    | 4.8        | (16)          | 3.3             |
| >270 days but <= 1 year   | 135                    | 3.1        | (20)          | 4.0             |
| >1 year                   | 1,305                  | 29.7       | (261)         | 52.6            |
| Total                     | \$ 4,386               | 100.0%     | \$ (496)      | 100.0%          |

For the three and six months ended June 30, 2014, we sold or otherwise disposed of securities in an unrealized loss position with a fair value (proceeds) of \$1.6 million and \$4.4 million, respectively. The loss realized on the sale of these securities was \$0.2 million and \$0.5 million, respectively. We made the decision to exit these holdings in conjunction with our overall asset liability management process.

For the three and six months ended June 30, 2014, we sold securities in an unrealized gain position with a fair value of \$306.3 million and \$571.0 million, respectively. The gain realized on the sale of these securities was \$20.4 million and \$28.1 million, respectively.

The \$1.0 million of other realized losses recognized for the three months ended June 30, 2014, consists of the decrease in the mortgage loan reserves of \$0.2 million, mortgage loan losses of \$1.0 million, real estate losses of \$0.3 million, and partnership gains of \$0.1 million. The \$2.6 million of other realized losses recognized for the six months ended June 30, 2014, consists of the increase in the mortgage loan reserves of \$1.2 million, mortgage loan losses of \$1.0 million, real estate losses of \$0.3 million, and partnership losses of \$0.1 million.

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For the three and six months ended June 30, 2014, net gains of \$61.0 million and \$127.3 million primarily related to changes in fair value on our Modco trading portfolios were included in realized gains and losses, respectively. Of this amount, approximately \$6.1 million and \$11.8 million, respectively, of gains were realized through the sale of certain securities, which will be reimbursed to our reinsurance partners over time through the reinsurance settlement process for this block of business. The Modco embedded derivative associated with the trading portfolios had realized pre-tax losses of \$52.2 million and \$112.4 million during the three and six months ended June 30, 2014, respectively. These losses were primarily the result of credit spreads modestly tightening and lower treasury yields.



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Realized investment gains and losses related to derivatives represent changes in their fair value during the period and termination gains/(losses) on those derivatives that were closed during the period.

We use equity, interest rate, currency, and volatility futures to mitigate the risk related to certain guaranteed minimum benefits, including GMWB, within our VA products. In general, the cost of such benefits varies with the level of equity and interest rate markets, foreign currency levels, and overall volatility. The equity futures resulted in net pre-tax losses of \$7.3 million and \$9.9 million, interest rate futures resulted in pre-tax gains of \$6.5 million and \$10.8 million, currency futures resulted in net pre-tax losses of \$2.9 million and \$4.2 million, and volatility futures resulted in no pre-tax gains or losses for the three and six months ended June 30, 2014, respectively. No volatility future positions were held as of June 30, 2014.

We also use equity options, variance swaps, and volatility options to mitigate the risk related to certain guaranteed minimum benefits, including GMWB, within our VA products. In general, the cost of such benefits varies with the level of equity markets and overall volatility. The equity options resulted in net pre-tax losses of \$20.9 million and \$33.3 million, the variance swaps resulted in a net pre-tax loss of \$0.8 million and \$2.7 million, and the volatility options resulted in no pre-tax gains or losses, respectively, for three and six months ended June 30, 2014. No volatility options positions were held as of June 30, 2014.

We use interest rate swaps and interest rate swaptions to mitigate the risk related to certain guaranteed minimum benefits, including GMWB, within our VA products. The interest rate swaps resulted in net pre-tax gains of \$45.2 million and \$102.5 million and interest rate swaptions resulted in a net pre-tax loss of \$5.0 million and \$14.4 million for the three and six months ended June 30, 2014, respectively.

The GMWB rider embedded derivative on variable deferred annuities, with a GMWB rider, had net realized losses of \$47.4 million and \$129.7 million for the three and six months ended June 30, 2014, respectively. The loss was primarily the result of a change in interest rates during 2014.

We use certain interest rate swaps to mitigate the price volatility of fixed maturities. These positions resulted in no pre-tax gains or losses for the three and six months ended June 30, 2014. None of these positions were held as of June 30, 2014.

We purchased interest rate caps during 2011, to mitigate our credit risk with respect to our LIBOR exposure and the potential impact of European financial market distress. These caps resulted in no pre-tax gains or losses for the three and six months ended June 30, 2014. No interest rate caps were held as of June 30, 2014.

We also use various swaps and other types of derivatives to mitigate risk related to other exposures. These contracts generated net pre-tax losses of \$0.1 million and \$0.2 million for the three and six months ended June 30, 2014, respectively.

We recognized pre-tax losses of \$8.3 million and \$6.6 million, respectively, for the three and six months ended June 30, 2014 related to the embedded derivative on the FIA product. We use certain equity options as well as equity and volatility futures to mitigate certain equity market risks associated with the FIA. For the three and six months ended June 30, 2014, we recognized pre-tax gains of \$3.6 million and \$4.9 million

related to these derivatives, respectively.

We recognized pre-tax losses of \$0.3 million for the three and six months ended June 30, 2014 related to the embedded derivative on the indexed universal life ( IUL ) product.

**Unrealized Gains and Losses Available-for-Sale Securities**

The information presented below relates to investments at a certain point in time and is not necessarily indicative of the status of the portfolio at any time after June 30, 2014. Information about unrealized gains and losses is subject to rapidly changing conditions, including volatility of financial markets and changes in interest rates. Management considers a number of factors in determining if an unrealized loss is other-than-temporary, including the expected cash to be collected and the intent, likelihood, and/or ability to hold the security until recovery. Consistent with our long-standing practice, we do not utilize a bright line test to determine other-than-

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temporary impairments. On a quarterly basis, we perform an analysis on every security with an unrealized loss to determine if an other-than-temporary impairment has occurred. This analysis includes reviewing several metrics including collateral, expected cash flows, ratings, and liquidity. Furthermore, since the timing of recognizing realized gains and losses is largely based on management's decisions as to the timing and selection of investments to be sold, the tables and information provided below should be considered within the context of the overall unrealized gain/(loss) position of the portfolio. We had an overall net unrealized gain of \$2.9 billion, prior to tax and DAC offsets, as of June 30, 2014, and an overall net unrealized gain of \$1.1 billion as of December 31, 2013.

For fixed maturity and equity securities held that are in an unrealized loss position as of June 30, 2014, the fair value, amortized cost, unrealized loss, and total time period that the security has been in an unrealized loss position are presented in the table below:

|                           | Fair<br>Value | % Fair<br>Value | Amortized<br>Cost | % Amortized<br>Cost | Unrealized<br>Loss | % Unrealized<br>Loss |
|---------------------------|---------------|-----------------|-------------------|---------------------|--------------------|----------------------|
| (Dollars In Thousands)    |               |                 |                   |                     |                    |                      |
| <= 90 days                | \$ 1,110,750  | 26.5%           | \$ 1,150,369      | 26.3%               | \$ (39,619)        | 23.4%                |
| >90 days but <= 180 days  | 56,765        | 1.4             | 57,827            | 1.3                 | (1,062)            | 0.6                  |
| >180 days but <= 270 days | 56,020        | 1.3             | 57,708            | 1.3                 | (1,688)            | 1.0                  |
| >270 days but <= 1 year   | 365,867       | 8.7             | 377,723           | 8.7                 | (11,856)           | 7.0                  |
| >1 year but <= 2 years    | 1,902,204     | 45.3            | 1,975,530         | 45.2                | (73,326)           | 43.2                 |
| >2 years but <= 3 years   | 381,295       | 9.1             | 397,973           | 9.1                 | (16,678)           | 9.8                  |
| >3 years but <= 4 years   | 30,133        | 0.7             | 33,038            | 0.8                 | (2,905)            | 1.7                  |
| >4 years but <= 5 years   | 18,349        | 0.4             | 20,007            | 0.5                 | (1,658)            | 1.0                  |
| >5 years                  | 275,105       | 6.6             | 295,884           | 6.8                 | (20,779)           | 12.3                 |
| Total                     | \$ 4,196,488  | 100.0%          | \$ 4,366,059      | 100.0%              | \$ (169,571)       | 100.0%               |

The majority of the unrealized loss as of June 30, 2014 for both investment grade and below investment grade securities is attributable to fluctuations in credit and mortgage spreads for certain securities. The negative impact of spread levels for certain securities was partially offset by lower treasury yield levels and the associated positive effect on security prices. Spread levels have improved since December 31, 2013. However, certain types of securities, including tranches of RMBS and ABS, continue to be priced at a level which has caused the unrealized losses noted above. We believe spread levels on these RMBS and ABS are largely due to uncertainties regarding future performance of the underlying mortgage loans and/or assets.

As of June 30, 2014, the Barclays Investment Grade Index was priced at 97.1 bps versus a 10 year average of 164.7 bps. Similarly, the Barclays High Yield Index was priced at 373.4 bps versus a 10 year average of 601.6 bps. As of June 30, 2014, the five, ten, and thirty-year U.S. Treasury obligations were trading at levels of 1.631%, 2.531%, and 3.360%, as compared to 10 year averages of 2.608%, 3.413%, and 4.143%, respectively.

As of June 30, 2014, 83.2% of the unrealized loss was associated with securities that were rated investment grade. We have examined the performance of the underlying collateral and cash flows and expect that our investments will continue to perform in accordance with their contractual terms. Factors such as credit enhancements within the deal structures and the underlying collateral performance/characteristics support the recoverability of the investments. Based on the factors discussed, we do not consider these unrealized loss positions to be other-than-temporary. However, from time to time, we may sell securities in the ordinary course of managing our portfolio to meet diversification, credit quality, yield enhancement, asset/liability management, and liquidity requirements.

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Expectations that investments in mortgage-backed and asset-backed securities will continue to perform in accordance with their contractual terms are based on assumptions a market participant would use in determining the current fair value. It is reasonably possible that the underlying collateral of these investments will perform worse than current market expectations and that such an event may lead to adverse changes in the cash flows on our holdings of these types of securities. This could lead to potential future write-downs within our portfolio of mortgage-backed and asset-backed securities. Expectations that our investments in corporate securities and/or debt obligations will continue to perform in accordance with their contractual terms are based on evidence gathered through our normal credit surveillance process. Although we do not anticipate such events, it is reasonably possible that issuers of our investments in corporate securities will perform worse than current expectations. Such events may lead us to recognize potential

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future write-downs within our portfolio of corporate securities. It is also possible that such unanticipated events would lead us to dispose of those certain holdings and recognize the effects of any such market movements in our financial statements.

As of June 30, 2014, there were estimated gross unrealized losses of \$7.7 million related to our mortgage-backed securities collateralized by Alt-A mortgage loans. Gross unrealized losses in our securities collateralized by Alt-A residential mortgage loans as of June 30, 2014, were primarily the result of continued widening spreads, representing marketplace uncertainty arising from higher defaults in Alt-A residential mortgage loans and rating agency downgrades of securities collateralized by Alt-A residential mortgage loans. As of June 30, 2014, we reviewed the performance of the underlying collateral supporting these securities and determined that the expected cash flows were in line with the valuation. As such, we believe unrealized losses as of June 30, 2014 were temporary in nature.

We have no material concentrations of issuers or guarantors of fixed maturity securities. The industry segment composition of all securities in an unrealized loss position held as of June 30, 2014, is presented in the following table:

|   | Fair Value             | % Fair Value | Amortized Cost | % Amortized Cost | Unrealized Loss | % Unrealized Loss |
|---|------------------------|--------------|----------------|------------------|-----------------|-------------------|
|   | (Dollars In Thousands) |              |                |                  |                 |                   |
| Banking   | \$ 288,440             | 6.9%         | \$ 306,108     | 7.0%             | \$ (17,668)     | 10.4%             |
| Other finance                                     | 111,253                | 2.7          | 113,172        | 2.6              | (1,919)         | 1.1               |
| Electric  | 176,919                | 4.2          | 181,982        | 4.2              | (5,063)         | 3.0               |
| Natural gas                                       | 130,056                | 3.1          | 134,175        | 3.1              | (4,119)         | 2.4               |
| Insurance   | 140,556                | 3.3          | 144,760        | 3.3              | (4,204)         | 2.5               |
| Energy  | 85,842                 | 2.0          | 87,554         | 2.0              | (1,712)         | 1.0               |
| Communications                                    | 179,238                | 4.3          | 186,832        | 4.3              | (7,594)         | 4.5               |
| Basic industrial                                  | 197,959                | 4.7          | 207,607        | 4.8              | (9,648)         | 5.7               |
| Consumer noncyclical                              | 450,559                | 10.7         | 468,662        | 10.7             | (18,103)        | 10.7              |
| Consumer cyclical                                 | 201,903                | 4.8          | 209,705        | 4.8              | (7,802)         | 4.6               |
| Finance companies                                 | 2,580                  | 0.1          | 2,993          | 0.1              | (413)           | 0.2               |
| Capital goods                                     | 95,585                 | 2.3          | 98,820         | 2.3              | (3,235)         | 1.9               |
| Transportation                                    | 75,865                 | 1.8          | 78,834         | 1.8              | (2,969)         | 1.8               |
| Other industrial                                  | 91,134                 | 2.2          | 93,328         | 2.1              | (2,194)         | 1.3               |
| Brokerage   |                        |              |                |                  |                 |                   |
| Technology  | 159,814                | 3.8          | 166,337        | 3.8              | (6,523)         | 3.8               |
| Real estate                                       |                        |              |                |                  |                 |                   |
| Other utility                                     | 7,534                  | 0.2          | 7,639          | 0.2              | (105)           | 0.1               |
| Commercial mortgage-backed securities             | 163,157                | 3.9          | 167,180        | 3.8              | (4,023)         | 2.4               |
| Other asset-backed securities                     | 645,847                | 15.4         | 678,694        | 15.5             | (32,847)        | 19.4              |
| Residential mortgage-backed non-agency securities | 201,949                | 4.8          | 213,761        | 4.9              | (11,812)        | 7.0               |
| Residential mortgage-backed agency securities     | 38,194                 | 0.9          | 40,354         | 0.9              | (2,160)         | 1.3               |
| U.S. government-related securities                | 709,698                | 16.9         | 731,483        | 16.8             | (21,785)        | 12.8              |
| Other government-related securities               |                        |              |                |                  |                 |                   |
| States, municipals, and political divisions       | 42,406                 | 1.0          | 46,079         | 1.0              | (3,673)         | 2.1               |
| Total   | \$ 4,196,488           | 100.0%       | \$ 4,366,059   | 100.0%           | \$ (169,571)    | 100.0%            |



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The percentage of our unrealized loss positions, segregated by industry segment, is presented in the following table:

|   | June 30, 2014 | As of<br>December 31, 2013 |
|---|---------------|----------------------------|
| Banking   | 10.4%         | 8.1%                       |
| Other finance                                     | 1.1           | 2.3                        |
| Electric  | 3.0           | 7.0                        |
| Natural gas                                       | 2.4           | 5.1                        |
| Insurance   | 2.5           | 4.2                        |
| Energy  | 1.0           | 2.4                        |
| Communications                                    | 4.5           | 5.6                        |
| Basic industrial                                  | 5.7           | 5.1                        |
| Consumer noncyclical                              | 10.7          | 12.1                       |
| Consumer cyclical                                 | 4.6           | 6.1                        |
| Finance companies                                 | 0.2           | 0.2                        |
| Capital goods                                     | 1.9           | 2.8                        |
| Transportation                                    | 1.8           | 2.4                        |
| Other industrial                                  | 1.3           | 1.6                        |
| Brokerage   |               | 0.7                        |
| Technology  | 3.8           | 3.9                        |
| Real estate                                       |               | 0.6                        |
| Other utility                                     | 0.1           | 0.7                        |
| Commercial mortgage-backed securities             | 2.4           | 3.3                        |
| Other asset-backed securities                     | 19.4          | 11.5                       |
| Residential mortgage-backed non-agency securities | 7.0           | 2.5                        |
| Residential mortgage-backed agency securities     | 1.3           | 1.6                        |
| U.S. government-related securities                | 12.8          | 8.9                        |
| Other government-related securities               |               |                            |
| States, municipals, and political divisions       | 2.1           | 1.3                        |
| Total   | 100.0%        | 100.0%                     |

The range of maturity dates for securities in an unrealized loss position as of June 30, 2014, varies, with 5.1% maturing in less than 5 years, 31.7% maturing between 5 and 10 years, and 63.2% maturing after 10 years. The following table shows the credit rating of securities in an unrealized loss position as of June 30, 2014:

| S&P or Equivalent Designation | Fair Value   | % Fair Value | Amortized Cost<br>(Dollars In Thousands) | % Amortized Cost | Unrealized Loss | % Unrealized Loss |
|-------------------------------|--------------|--------------|--|------------------|-----------------|-------------------|
| AAA/AA/A                      | \$ 2,417,808 | 57.6%        | \$ 2,514,465                             | 57.6%            | \$ (96,657)     | 57.0%             |
| BBB                           | 1,291,303    | 30.8         | 1,335,736                                | 30.6             | (44,433)        | 26.2              |
| Investment grade              | 3,709,111    | 88.4         | 3,850,201                                | 88.2             | (141,090)       | 83.2              |
| BB                            | 163,185      | 3.9          | 174,648                                  | 4.0              | (11,463)        | 6.8               |
| B                             | 50,927       | 1.2          | 52,815                                   | 1.2              | (1,888)         | 1.1               |
| CCC or lower                  | 273,265      | 6.5          | 288,395                                  | 6.6              | (15,130)        | 8.9               |
| Below investment grade        | 487,377      | 11.6         | 515,858                                  | 11.8             | (28,481)        | 16.8              |
| Total                         | \$ 4,196,488 | 100.0%       | \$ 4,366,059                             | 100.0%           | \$ (169,571)    | 100.0%            |

As of June 30, 2014, we held a total of 390 positions that were in an unrealized loss position. Included in that amount were 88 positions of below investment grade securities with a fair value of \$515.9 million that were in an unrealized loss position. Total unrealized losses related to below

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investment grade securities were \$28.5 million, of which \$16.8 million had been in an unrealized loss position for more than twelve months. Below investment grade securities in an unrealized loss position were 1.1% of invested assets.



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As of June 30, 2014, securities in an unrealized loss position that were rated as below investment grade represented 11.6% of the total fair value and 16.8% of the total unrealized loss. After a review of each security and its expected cash flows, we believe the decline in market value to be temporary. We have the ability and intent to hold these securities to maturity. As of June 30, 2014, total unrealized losses for all securities in an unrealized loss position for more than twelve months were \$115.3 million. A widening of credit spreads is estimated to account for unrealized losses of \$446.7 million, with changes in treasury rates offsetting this loss by an estimated \$331.4 million.

The majority of our RMBS holdings as of June 30, 2014, were super senior or senior bonds in the capital structure. Our total non-agency portfolio has a weighted-average life of 6.91 years. The following table categorizes the weighted-average life for our non-agency portfolio, by category of material holdings, as of June 30, 2014:

| Non-agency portfolio | Weighted-Average<br>Life |
|----------------------|--------------------------|
| Prime                | 8.10                     |
| Alt-A                | 5.47                     |

The following table includes the fair value, amortized cost, unrealized loss, and total time period that the security has been in an unrealized loss position for all below investment grade securities as of June 30, 2014:

|                           | Fair<br>Value | % Fair<br>Value | Amortized<br>Cost | % Amortized<br>Cost | Unrealized<br>Loss | % Unrealized<br>Loss |
|---------------------------|---------------|-----------------|-------------------|---------------------|--------------------|----------------------|
| (Dollars In Thousands)    |               |                 |                   |                     |                    |                      |
| <= 90 days                | \$ 185,365    | 38.0%           | \$ 194,552        | 37.7%               | \$ (9,187)         | 32.3%                |
| >90 days but <= 180 days  | 11,406        | 2.3             | 11,455            | 2.2                 | (49)               | 0.2                  |
| >180 days but <= 270 days | 6,319         | 1.3             | 6,925             | 1.3                 | (606)              | 2.1                  |
| >270 days but <= 1 year   | 51,690        | 10.6            | 53,495            | 10.4                | (1,805)            | 6.3                  |
| >1 year but <= 2 years    | 44,829        | 9.2             | 48,973            | 9.5                 | (4,144)            | 14.6                 |
| >2 years but <= 3 years   | 29,374        | 6.0             | 31,156            | 6.0                 | (1,782)            | 6.3                  |
| >3 years but <= 4 years   | 17,608        | 3.6             | 18,038            | 3.5                 | (430)              | 1.5                  |
| >4 years but <= 5 years   | 18,349        | 3.8             | 20,007            | 3.9                 | (1,658)            | 5.8                  |
| >5 years                  | 122,437       | 25.2            | 131,257           | 25.5                | (8,820)            | 30.9                 |
| Total                     | \$ 487,377    | 100.0%          | \$ 515,858        | 100.0%              | \$ (28,481)        | 100.0%               |

**LIQUIDITY AND CAPITAL RESOURCES****Liquidity**

Liquidity refers to a company's ability to generate adequate amounts of cash to meet its needs. We meet our liquidity requirements primarily through positive cash flows from our operating subsidiaries. Primary sources of cash from the operating subsidiaries are premiums, deposits for policyholder accounts, investment sales and maturities, and investment income. Primary uses of cash include benefit payments, withdrawals from policyholder accounts, investment purchases, policy acquisition costs, interest payments, and other operating expenses. We believe that we have sufficient liquidity to fund our cash needs under normal operating scenarios.

In the event of significant unanticipated cash requirements beyond our normal liquidity needs, we have additional sources of liquidity available depending on market conditions and the amount and timing of the liquidity need. These additional sources of liquidity include cash flows from operations, the sale of liquid assets, accessing our credit facility, and other sources described herein.

Our decision to sell investment assets could be impacted by accounting rules, including rules relating to the likelihood of a requirement to sell securities before recovery of our cost basis. Under stressful market and economic conditions, liquidity may broadly deteriorate which could negatively impact our ability to sell investment assets. If we require on short notice significant amounts of cash in excess of normal requirements, we may have difficulty selling

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investment assets in a timely manner, be forced to sell them for less than we otherwise would have been able to realize, or both.

While we anticipate that the cash flows of our operating subsidiaries will be sufficient to meet our investment commitments and operating cash needs in a normal credit market environment, we recognize that investment commitments scheduled to be funded may, from time to time, exceed the funds then available. Therefore, we have established repurchase agreement programs for certain of our insurance subsidiaries to provide liquidity when needed. We expect that the rate received on our investments will equal or exceed our borrowing rate. Under this program, we may, from time to time, sell an investment security at a specific price and agree to repurchase that security at another specified price at a later date. These borrowings are for a term less than 90 days. The market value of securities to be repurchased is monitored and collateral levels are adjusted where appropriate to protect the counterparty against credit exposure. The agreements provide for net settlement in the event of default or on termination of the agreements. As of June 30, 2014, the fair value of securities pledged under the repurchase program was \$476.3 million and the repurchase obligation of \$420.5 million was included in our consolidated condensed balance sheets (at an average borrowing rate of 11 basis points). During the six months ended June 30, 2014, the maximum balance outstanding at any one point in time related to these programs was \$633.7 million. The average daily balance was \$510.2 million (at an average borrowing rate of 10 basis points) during the six months ended June 30, 2014. As of December 31, 2013, we had a \$350.0 million outstanding balance related to such borrowings. During 2013, the maximum balance outstanding at any one point in time related to these programs was \$815.0 million. The average daily balance was \$496.9 million (at an average borrowing rate of 11 basis points) during the year ended December 31, 2013.

Additionally, we may, from time to time, sell short-duration stable value products to complement our cash management practices. Depending on market conditions, we may also use securitization transactions involving our commercial mortgage loans to increase liquidity for the operating subsidiaries.

**Credit Facility**

We have access to a Credit Facility that provides the ability to borrow on an unsecured basis up to an aggregate principal amount of \$750 million. We have the right in certain circumstances to request that the commitment under the Credit Facility be increased up to a maximum principal amount of \$1.0 billion. Balances outstanding under the Credit Facility accrue interest at a rate equal to, at the option of the Borrowers, (i) LIBOR plus a spread based on the ratings of our senior unsecured long-term debt ( Senior Debt ), or (ii) the sum of (A) a rate equal to the highest of (x) the Administrative Agent's prime rate, (y) 0.50% above the Federal Funds rate, or (z) the one-month LIBOR plus 1.00% and (B) a spread based on the ratings of our Senior Debt. The Credit Facility also provides for a facility fee at a rate, currently 0.175%, that varies with the ratings of our Senior Debt and that is calculated on the aggregate amount of commitments under the Credit Facility, whether used or unused. The maturity date on the Credit Facility is July 17, 2017. We were not aware of any non-compliance with the financial debt covenants of the Credit Facility as of June 30, 2014. There was an outstanding balance of \$345.0 million at an interest rate of LIBOR plus 1.20% under the Credit Facility as of June 30, 2014.

**Sources and Use of Cash**

Our primary sources of funding are dividends from our operating subsidiaries; revenues from investments, data processing, legal, and management services rendered to subsidiaries; investment income; and external financing. These sources of cash support our general corporate needs including our common stock dividends and debt service. The states in which our insurance subsidiaries are domiciled impose certain restrictions on the insurance subsidiaries' ability to pay us dividends. These restrictions are based in part on the prior year's statutory income and/or surplus. Generally, these restrictions pose no short-term liquidity concerns. We plan to retain portions of the earnings of our insurance subsidiaries in those companies primarily to support their future growth.

We are a member of the FHLB of Cincinnati. FHLB advances provide an attractive funding source for short-term borrowing and for the sale of funding agreements. Membership in the FHLB requires that we purchase FHLB capital stock based on a minimum requirement and a percentage of the dollar amount of advances outstanding. Our borrowing capacity is determined by the following factors: 1) total advance capacity is limited to the lower of 50% of total assets or 100% of mortgage-related assets of Protective Life Insurance Company, our largest insurance subsidiary, 2) ownership of appropriate capital and activity stock to support continued membership in the FHLB and current and

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future advances, and 3) the availability of adequate eligible mortgage or treasury/agency collateral to back current and future advances.

We held \$66.4 million of FHLB common stock as of June 30, 2014, which is included in equity securities. In addition, our obligations under the advances must be collateralized. We maintain control over any such pledged assets, including the right of substitution. As of June 30, 2014, we had \$821.9 million of funding agreement-related advances and accrued interest outstanding under the FHLB program.

As of June 30, 2014, we reported approximately \$617.0 million (fair value) of Auction Rate Securities ( ARS ) in non-Modco portfolios. As of June 30, 2014, 100% of these ARS were rated Aaa/AA+. While the auction rate market has experienced liquidity constraints, we believe that based on our current liquidity position and our operating cash flows, any lack of liquidity in the ARS market will not have a material impact on our liquidity, financial condition, or cash flows.

All of the auction rate securities held, on a consolidated basis, in non-Modco portfolios as of June 30, 2014, were student loan-backed auction rate securities, for which the underlying collateral is at least 97% guaranteed by the Federal Family Education Loan Program ( FFELP ). As there is no active market for these auction rate securities, we use a valuation model, which incorporates, among other inputs, the contractual terms of each indenture and current valuation information from actively-traded asset-backed securities with comparable underlying assets (i.e. FFELP-backed student loans) and vintage.

We use an income approach valuation model to determine the fair value of our student loan-backed auction rate securities. Specifically, a discounted cash flow method is used. The expected yield on the auction rate securities is estimated for each coupon date, based on the contractual terms on each indenture. The estimated market yield is based on comparable securities with observable yields and an additional yield spread for illiquidity of auction rate securities in the current market.

The auction rate securities held in non-Modco portfolios are classified as a Level 2 or Level 3 valuation. An unrealized loss of \$25.5 million and \$57.2 million was recorded as of June 30, 2014 and December 31, 2013, respectively, and we have not recorded any other-than-temporary impairment because the underlying collateral for each of the auction rate securities is at least 97% guaranteed by the FFELP and there are subordinate tranches within each of these auction rate security issuances that would support the senior tranches in the event of default. In the event of a complete and total default by all underlying student loans, the principal shortfall, in excess of the 97% FFELP guarantee, would be absorbed by the subordinate tranches. Our credit exposure is to the FFELP guarantee, not the underlying student loans. At this time, we have no reason to believe that the U.S. Department of Education would not honor the FFELP guarantee, if it were necessary. In addition, we do not intend to sell or expect to be required to sell the securities before recovering our amortized cost of these securities. Therefore, we believe that no other-than-temporary impairment has been experienced.

The liquidity requirements of our regulated insurance subsidiaries primarily relate to the liabilities associated with their various insurance and investment products, operating expenses, and income taxes. Liabilities arising from insurance and investment products include the payment of policyholder benefits, as well as cash payments in connection with policy surrenders and withdrawals, policy loans, and obligations to redeem funding agreements.

Our insurance subsidiaries maintain investment strategies intended to provide adequate funds to pay benefits and expected surrenders, withdrawals, loans, and redemption obligations without forced sales of investments. In addition, our insurance subsidiaries hold highly liquid,

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high-quality short-term investment securities and other liquid investment grade fixed maturity securities to fund our expected operating expenses, surrenders, and withdrawals. As of June 30, 2014, our total cash and invested assets were \$46.5 billion. The life insurance subsidiaries were committed as of June 30, 2014, to fund mortgage loans in the amount of \$489.6 million.

Our positive cash flows from operations are used to fund an investment portfolio that provides for future benefit payments. We employ a formal asset/liability program to manage the cash flows of our investment portfolio relative to our long-term benefit obligations. Our insurance subsidiaries held approximately \$458.4 million in cash and short-term investments as of June 30, 2014, and we held \$56.1 million in cash available for general corporate purposes.

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The following chart includes the cash flows provided by or used in operating, investing, and financing activities for the following periods:

|   | <b>For The<br/>Six Months Ended<br/>June 30,</b> |              |
|---|--|--------------|
|   | <b>2014</b>                                      | <b>2013</b>  |
|   | <b>(Dollars In Thousands)</b>                    |              |
| Net cash provided by operating activities           | \$ 423,490                                       | \$ 191,367   |
| Net cash used in investing activities               | (513,536)  | (769,045)    |
| Net cash (used in) provided by financing activities | (15,408)   | 464,589      |
| Total   | \$ (105,454)                                     | \$ (113,089) |

*For The Six Months Ended June 30, 2014 as compared to The Six Months Ended June 30, 2013*

**Net cash provided by operating activities** - Cash flows from operating activities are affected by the timing of premiums received, fees received, investment income, and expenses paid. Principal sources of cash include sales of our products and services. We typically generate positive cash flows from operating activities, as premiums and deposits collected from our insurance and investment products exceed benefit payments and redemptions, and we invest the excess. Accordingly, in analyzing our cash flows we focus on the change in the amount of cash available and used in investing activities.

**Net cash used in investing activities** - Changes in cash from investing activities primarily related to the activity in our investment portfolio.

**Net cash (used in) provided by financing activities** - Changes in cash from financing activities included \$70.5 million inflows from repurchase program borrowings for the six months ended June 30, 2014 as compared to \$190.0 million for the six months ended June 30, 2013 and \$72.1 million inflows of investment product and universal life net activity for the six months ended June 30, 2014, as compared to \$225.5 million of inflows in the prior year. Net activity related to credit facility borrowings resulted in outflows of \$140.0 million for the six months ended June 30, 2014, as compared to net inflows of \$60.0 million for the six months ended June 30, 2013. Net issuance of non-recourse funding obligations equaled \$16.6 million during the six months ended June 30, 2014, as compared to issuance of \$18.9 million during the six months ended June 30, 2013.

**Capital Resources**

To give us flexibility in connection with future acquisitions and other funding needs, we have debt securities, preferred and common stock, and additional preferred securities of special purpose finance subsidiaries registered under the Securities Act of 1933 on a delayed (or shelf) basis. Additionally, we have access to the Credit Facility previously mentioned.

**Captive Reinsurance Companies**

Golden Gate Captive Insurance Company ( Golden Gate ), a South Carolina special purpose financial captive insurance company and wholly owned subsidiary of PLICO, had three series of Surplus Notes with a total outstanding balance of \$800 million as of June 30, 2014. We hold the entire outstanding balance of Surplus Notes. The Series A1 Surplus Notes have a balance of \$400 million and accrue interest at 7.375%, the Series A2 Surplus Notes have a balance of \$100 million and accrue interest at 8%, and the Series A3 Surplus Notes have a balance of \$300 million and accrue interest at 8.45%.

Golden Gate II Captive Insurance Company ( Golden Gate II ), a special purpose financial captive insurance company wholly owned by PLICO, had \$575 million of outstanding non-recourse funding obligations as of June 30, 2014. These outstanding non-recourse funding obligations were issued to special purpose trusts, which in turn issued securities to third parties. Certain of our affiliates own a portion of these securities. As of June 30, 2014, securities



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related to \$176.6 million of the outstanding balance of the non-recourse funding obligations were held by external parties and securities related to \$398.4 million of the non-recourse funding obligations were held by our affiliates. These non-recourse funding obligations mature in 2052. \$275 million of this amount is currently accruing interest at a rate of LIBOR plus 30 basis points. We have experienced higher borrowing costs than were originally expected associated with \$300 million of our non-recourse funding obligations supporting the business reinsured to Golden Gate II. These higher costs are the result of a higher spread component of interest expense associated with the illiquidity of the current market for auction rate securities, as well as a rating downgrade of our guarantor by certain rating agencies. The current rate associated with these obligations is LIBOR plus 200 basis points, which is the maximum rate we can be required to pay under these obligations. We have contingent approval to issue an additional \$100 million of obligations. Under the terms of the non-recourse funding obligations, the special purpose trusts, as holders of the non-recourse funding obligations, cannot require repayment from us or any of our subsidiaries, other than Golden Gate II, the direct issuer of the non-recourse funding obligations, although we have agreed to indemnify Golden Gate II for certain costs and obligations (which obligations do not include payment of principal and interest on the surplus notes). In addition, we have entered into certain support agreements with Golden Gate II obligating us to make capital contributions or provide support related to certain of Golden Gate II's expenses and in certain circumstances, to collateralize certain of our obligations to Golden Gate II. These support agreements provide that amounts would become payable by us to Golden Gate II if its annual general corporate expenses were higher than modeled amounts or if Golden Gate II's investment income on certain investments or premium income was below certain actuarially determined amounts. As of June 30, 2014, no payments have been made under these agreements.

On October 10, 2012, Golden Gate V Vermont Captive Insurance Company (Golden Gate V) and Red Mountain, LLC (Red Mountain), indirect wholly owned subsidiaries of the Company, entered into a 20-year transaction to finance up to \$945 million of AXXX reserves related to a block of universal life insurance policies with secondary guarantees issued by our direct wholly owned subsidiary PLICO and indirect wholly owned subsidiary, WCL. Golden Gate V issued non-recourse funding obligations to Red Mountain, and Red Mountain issued a note with an initial principal amount of \$275 million, increasing to a maximum of \$945 million in 2027, to Golden Gate V for deposit to a reinsurance trust supporting Golden Gate V's obligations under a reinsurance agreement with WCL, pursuant to which WCL cedes liabilities relating to the policies of WCL and retrocedes liabilities relating to the policies of PLICO. Through the structure, Hannover Life Reassurance Company of America (Hannover Re), the ultimate risk taker in the transaction, provides credit enhancement to the Red Mountain note for the 20-year term in exchange for a fee. The transaction is non-recourse to Golden Gate V, Red Mountain, WCL, PLICO and the Company, meaning that none of these companies are liable for the reimbursement of any credit enhancement payments required to be made. As of June 30, 2014, the principal balance of the Red Mountain note was \$400 million. In connection with the transaction, we have entered into certain support agreements under which we guarantee or otherwise support certain obligations of Golden Gate V or Red Mountain. Future scheduled capital contributions to prefund credit enhancement fees amount to approximately \$144.3 million and will be paid in annual installments through 2031. The support agreements provide that amounts would become payable by us if Golden Gate V's annual general corporate expenses were higher than modeled amounts or in the event write-downs due to other-than-temporary impairments on assets held in certain accounts exceed defined threshold levels. Additionally, we have entered into separate agreements to indemnify Golden Gate V with respect to material adverse changes in non-guaranteed elements of insurance policies reinsured by Golden Gate V, and to guarantee payment of certain fee amounts in connection with the credit enhancement of the Red Mountain note. As of June 30, 2014, no payments have been made under these agreements.

**Letters of Credit**

Golden Gate III Vermont Captive Insurance Company (Golden Gate III), a Vermont special purpose financial insurance company and wholly owned subsidiary of PLICO, is party to a Reimbursement Agreement (the Reimbursement Agreement) with UBS AG, Stamford Branch (UBS), as issuing lender. Under the original Reimbursement Agreement, dated April 23, 2010, UBS issued a letter of credit (the LOC) in the initial amount of \$505 million to a trust for the benefit of WCL. The Reimbursement Agreement was subsequently amended and restated effective November 21, 2011 (the First Amended and Restated Reimbursement Agreement), to replace the existing LOC with one or more letters of credit from UBS, and to extend the maturity date from April 1, 2018, to April 1, 2022. On August 7, 2013, we entered into a Second Amended and Restated Reimbursement Agreement with UBS (the Second Amended and Restated Reimbursement Agreement), which amended and restated the First Amended and Restated Reimbursement Agreement. Under the Second and Amended and Restated Reimbursement Agreement a new LOC in an initial amount of \$710 million was issued by UBS in replacement of the existing LOC issued under the First



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Amended and Restated Reimbursement Agreement. The term of the LOC was extended from April 1, 2022 to October 1, 2023, subject to certain conditions being satisfied including scheduled capital contributions being made to Golden Gate III by one of its affiliates. The maximum stated amount of the LOC was increased from \$610 million to \$720 million in 2015 if certain conditions are met. On June 25, 2014, we entered into a Third Amended and Restated Reimbursement Agreement with UBS (the Third Amended and Restated Reimbursement Agreement), which amended and restated the Second Amended and Restated Reimbursement Agreement. Under the Third Amended and Restated Reimbursement Agreement, a new LOC in an initial amount of \$915 million was issued by UBS in replacement of the existing LOC issued under the Second Amended and Restated Reimbursement Agreement. The term of the LOC was extended from October 1, 2023 to April 1, 2025, subject to certain conditions being satisfied including scheduled capital contributions being made to Golden Gate III by one of its affiliates. The maximum stated amount of the LOC was increased from \$720 million to \$935 million in 2015 if certain conditions are met. The LOC is held in trust for the benefit of WCL, and supports certain obligations of Golden Gate III to WCL under an indemnity reinsurance agreement originally effective April 1, 2010, as amended and restated on November 21, 2011, and as further amended and restated on August 7, 2013 and on June 25, 2014 to include additional blocks of policies, and pursuant to which WCL cedes liabilities relating to the policies of WCL and retrocedes liabilities relating to the policies of PLICO. The LOC balance was \$915 million as of June 30, 2014. Subject to certain conditions, the amount of the LOC will be periodically increased up to a maximum of \$935 million in 2015. The term of the LOC is expected to be approximately 15 years from the original issuance date. This transaction is non-recourse to WCL, PLICO, and the Company, meaning that none of these companies other than Golden Gate III are liable for reimbursement on a draw of the LOC. We have entered into certain support agreements with Golden Gate III obligating us to make capital contributions or provide support related to certain of Golden Gate III's expenses and in certain circumstances, to collateralize certain of our obligations to Golden Gate III. Future scheduled capital contributions amount to approximately \$122.5 million and will be paid in three installments with the last payment occurring in 2021, and these contributions may be subject to potential offset against dividend payments as permitted under the terms of the Third Amended and Restated Reimbursement Agreement. The support agreements provide that amounts would become payable by us to Golden Gate III if its annual general corporate expenses were higher than modeled amounts or if specified catastrophic losses occur during defined time periods with respect to the policies reinsured by Golden Gate III. Pursuant to the terms of an amended and restated letter agreement with UBS, we have continued to guarantee the payment of fees to UBS as specified in the Third Amended and Restated Reimbursement Agreement. As of June 30, 2014, no payments have been made under these agreements.

Golden Gate IV Vermont Captive Insurance Company (Golden Gate IV), a Vermont special purpose financial insurance company and wholly owned subsidiary of PLICO, is party to a Reimbursement Agreement with UBS AG, Stamford Branch, as issuing lender. Under the Reimbursement Agreement, dated December 10, 2010, UBS issued an LOC in the initial amount of \$270 million to a trust for the benefit of WCL. The LOC balance increased, in accordance with the terms of the Reimbursement Agreement, during the second quarter of 2014 and was \$730 million as of June 30, 2014. Subject to certain conditions, the amount of the LOC will be periodically increased up to a maximum of \$790 million in 2016. The term of the LOC is expected to be 12 years from the original issuance date (stated maturity of December 30, 2022). The LOC was issued to support certain obligations of Golden Gate IV to WCL under an indemnity reinsurance agreement, pursuant to which WCL cedes liabilities related to the policies of WCL and retrocedes liabilities relating to the policies of PLICO. This transaction is non-recourse to WCL, PLICO, and the Company, meaning that none of these companies other than Golden Gate IV are liable for reimbursement on a draw of the LOC. We have entered into certain support agreements with Golden Gate IV obligating us to make capital contributions or provide support related to certain of Golden Gate IV's expenses and in certain circumstances, to collateralize certain of our obligations to Golden Gate IV. The support agreements provide that amounts would become payable by us to Golden Gate IV if its annual general corporate expenses were higher than modeled amounts or if specified catastrophic losses occur during defined time periods with respect to the policies reinsured by Golden Gate IV. We have also entered into a separate agreement to guarantee the payments of LOC fees under the terms of the Reimbursement Agreement. As of June 30, 2014, no payments have been made under these agreements.

A life insurance company's statutory capital is computed according to rules prescribed by the NAIC, as modified by state law. Generally speaking, other states in which a company does business defer to the interpretation of the domiciliary state with respect to NAIC rules, unless inconsistent with the other state's regulations. Statutory accounting rules are different from GAAP and are intended to reflect a more conservative view, for example, requiring immediate expensing of policy acquisition costs. The NAIC's risk-based capital requirements require insurance companies to calculate and report information under a risk-based capital formula. The achievement of long-term growth

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will require growth in the statutory capital of our insurance subsidiaries. The subsidiaries may secure additional statutory capital through various sources, such as retained statutory earnings or our equity contributions. In general, dividends up to specified levels are considered ordinary and may be paid thirty days after written notice to the insurance commissioner of the state of domicile unless such commissioner objects to the dividend prior to the expiration of such period. Dividends in larger amounts are considered extraordinary and are subject to affirmative prior approval by such commissioner. The maximum amount that would qualify as an ordinary dividend to us from our insurance subsidiaries in 2014 is estimated to be \$305.1 million.

State insurance regulators and the NAIC have adopted risk-based capital ( RBC ) requirements for life insurance companies to evaluate the adequacy of statutory capital and surplus in relation to investment and insurance risks. The requirements provide a means of measuring the minimum amount of statutory surplus appropriate for an insurance company to support its overall business operations based on its size and risk profile. A company's risk-based statutory surplus is calculated by applying factors and performing calculations relating to various asset, premium, claim, expense, and reserve items. Regulators can then measure the adequacy of a company's statutory surplus by comparing it to the RBC. We manage our capital consumption by using the ratio of our total adjusted capital, as defined by the insurance regulators, to our company action level RBC (known as the RBC ratio), also as defined by insurance regulators.

Statutory reserves established for VA contracts are sensitive to changes in the equity markets and are affected by the level of account values relative to the level of any guarantees and product design. As a result, the relationship between reserve changes and equity market performance may be non-linear during any given reporting period. Market conditions greatly influence the capital required due to their impact on the valuation of reserves and derivative investments mitigating the risk in these reserves. Risk mitigation activities may result in material and sometimes counterintuitive impacts on statutory surplus and RBC ratio. Notably, as changes in these market and non-market factors occur, both our potential obligation and the related statutory reserves and/or required capital can vary at a non-linear rate.

In an effort to mitigate the equity market risks discussed above relative to PLICO's RBC ratio, PLICO has reinsured GMWB and GMDB riders related to its variable annuity contracts to Shades Creek Captive Insurance Company ( Shades Creek ), a wholly owned insurance subsidiary. The purpose of Shades Creek is to reduce the volatility in RBC due to non-economic variables included within the RBC calculation.

We have an intercompany capital support agreement with Shades Creek. The agreement provides through a guarantee that we will contribute assets or purchase surplus notes (or cause an affiliate or third party to contribute assets or purchase surplus notes) in amounts necessary for Shades Creek's regulatory capital levels to equal or exceed minimum thresholds as defined by the agreement. As of June 30, 2014, Shades Creek maintained capital levels in excess of the required minimum thresholds. The maximum potential future payment amount which could be required under the capital support agreement will be dependent on numerous factors, including the performance of equity markets, the level of interest rates, performance of associated hedges, and related policyholder behavior.

We cede material amounts of insurance and transfer related assets to other insurance companies through reinsurance. However, notwithstanding the transfer of related assets, we remain liable with respect to ceded insurance should any reinsurer fail to meet the obligations that it assumed. We evaluate the financial condition of our reinsurers and monitor the associated concentration of credit risk. For the three and six months ended June 30, 2014, we ceded premiums to unaffiliated third party reinsurers amounting to \$343.0 million and \$670.7 million, respectively. In addition, we had receivables from unaffiliated reinsurers amounting to \$6.1 billion as of June 30, 2014. We review reinsurance receivable amounts for collectability and establish bad debt reserves if deemed appropriate.



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Various Nationally Recognized Statistical Rating Organizations ( rating organizations ) review the financial performance and condition of insurers, including our insurance subsidiaries, and publish their financial strength ratings as indicators of an insurer's ability to meet policyholder and contract holder obligations. These ratings are important to maintaining public confidence in an insurer's products, its ability to market its products and its competitive position. The following table summarizes the financial strength ratings of our significant member companies from the major independent rating organizations as of June 30, 2014:

| <b>Ratings</b>                                      | <b>A.M. Best</b> | <b>Fitch</b> | <b>Standard &amp; Poor's</b> | <b>Moody's</b> |
|---|------------------|--------------|------------------------------|----------------|
| <b>Insurance company financial strength rating:</b> |                  |              |                              |                |
| Protective Life Insurance Company                   | A+               | A            | AA-                          | A2             |
| West Coast Life Insurance Company                   | A+               | A            | AA-                          | A2             |
| Protective Life and Annuity Insurance Company       | A+               | A            | AA-                          |                |
| Lyndon Property Insurance Company                   | A-               |              |                              |                |
| MONY Life Insurance Company                         | A+               | A            | A+                           | A2             |

Our ratings are subject to review and change by the rating organizations at any time and without notice. A downgrade or other negative action by a ratings organization with respect to the financial strength ratings of our insurance subsidiaries could adversely affect sales, relationships with distributors, the level of policy surrenders and withdrawals, competitive position in the marketplace, and the cost or availability of reinsurance. With the announcement of the Dai-ichi transaction, each rating agency has undertaken a review of our insurance company subsidiaries' financial strength ratings in light of the transaction. The rating agencies may take various actions, positive or negative, and their actions may not be known until the Merger closes.

Rating organizations also publish credit ratings for the issuers of debt securities, including the Company. Credit ratings are indicators of a debt issuer's ability to meet the terms of debt obligations in a timely manner. These ratings are important in the debt issuer's overall ability to access credit markets and other types of liquidity. Ratings are not recommendations to buy our securities or products. A downgrade or other negative action by a ratings organization with respect to our credit rating could limit our access to capital markets, increase the cost of issuing debt, and a downgrade of sufficient magnitude, combined with other negative factors, could require us to post collateral. As is the case with the financial strength ratings of our insurance subsidiaries, the rating agencies have undertaken a review of our debt ratings in light of the Dai-ichi transaction.

**LIABILITIES**

Many of our products contain surrender charges and other features that are designed to reward persistency and penalize the early withdrawal of funds. Certain stable value and annuity contracts have market-value adjustments that protect us against investment losses if interest rates are higher at the time of surrender than at the time of issue.

As of June 30, 2014, we had policy liabilities and accruals of approximately \$31.4 billion. Our interest-sensitive life insurance policies have a weighted average minimum credited interest rate of approximately 3.51%.

**Contractual Obligations**

We enter into various obligations to third parties in the ordinary course of our operations. However, we do not believe that our cash flow requirements can be assessed solely based upon an analysis of these obligations. The most significant factors affecting our future cash flows are our ability to earn and collect cash from our customers, and the cash flows arising from our investment program. Future cash outflows, whether they are contractual obligations or not, will also vary based upon our future needs. Although some outflows are fixed, others depend on future events. Examples of fixed obligations include our obligations to pay principal and interest on fixed-rate borrowings. Examples of obligations that will vary include obligations to pay interest on variable-rate borrowings and insurance liabilities that

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depend on future interest rates, market performance, or surrender provisions. Many of our obligations are linked to cash-generating contracts. In addition, our operations involve significant expenditures that are not based upon contractual obligations. These include expenditures for income taxes and payroll.

As of June 30, 2014, we carried a \$135.0 million liability for uncertain tax positions, including interest on unrecognized tax benefits. These amounts are not included in the long-term contractual obligations table because of the difficulty in making reasonably reliable estimates of the occurrence or timing of cash settlements with the respective taxing authorities.

The table below sets forth future maturities of our contractual obligations:

|  | Total                | Payments due by period |                        |                     |                      |
|--|----------------------|------------------------|------------------------|---------------------|----------------------|
|  |                      | Less than<br>1 year    | 1-3 years              | 3-5 years           | More than<br>5 years |
|  |                      |                        | (Dollars In Thousands) |                     |                      |
| Debt(1)                                  | \$ 2,375,248         | \$ 229,566             | \$ 154,256             | \$ 626,095          | \$ 1,365,331         |
| Non-recourse funding obligations(2)      | 2,114,265            | 29,103                 | 71,100                 | 85,348              | 1,928,714            |
| Subordinated debt securities(3)          | 1,418,630            | 33,283                 | 66,566                 | 66,566              | 1,252,215            |
| Stable value products(4)                 | 2,515,119            | 934,221                | 1,000,612              | 500,094             | 80,192               |
| Operating leases(5)                      | 18,827               | 4,006                  | 9,403                  | 2,728               | 2,690                |
| Home office lease(6)                     | 80,503               | 1,224                  | 2,452                  | 76,827              |                      |
| Mortgage loan and investment commitments | 498,399              | 498,399                |                        |                     |                      |
| Repurchase program borrowings(7)         | 420,492              | 420,492                |                        |                     |                      |
| Policyholder obligations(8)              | 42,479,763           | 1,479,706              | 2,850,073              | 2,968,026           | 35,181,958           |
| <b>Total(9)</b>                          | <b>\$ 51,921,246</b> | <b>\$ 3,630,000</b>    | <b>\$ 4,154,462</b>    | <b>\$ 4,325,684</b> | <b>\$ 39,811,100</b> |

(1) Debt includes all principal amounts owed on note agreements and expected interest payments due over the term of the notes.

(2) Non-recourse funding obligations include all undiscounted principal amounts owed and expected future interest payments due over the term of the notes. Of the total undiscounted cash flows, \$1.9 billion relates to the Golden Gate V transaction. These cash out flows are matched and predominantly offset by the cash inflows Golden Gate V receives from notes issued by a nonconsolidated variable interest entity. The remaining amounts are associated with the Golden Gate II notes outstanding and held by third parties as well as certain obligations assumed with the acquisition of MONY Life Insurance Company.

(3) Subordinated debt securities includes all principal amounts and interest payments due over the term of the obligations.

(4) Anticipated stable value products cash flows including interest.

(5) Includes all lease payments required under operating lease agreements.

(6) The lease payments shown assume we exercise our option to purchase the building at the end of the lease term. Additionally, the payments due by the periods above were computed based on the terms of the renegotiated lease agreement, which was entered in December 2013.

(7) Represents secured borrowings as part of our repurchase program as well as related interest.

(8) Estimated contractual policyholder obligations are based on mortality, morbidity, and lapse assumptions comparable to our historical experience, modified for recent observed trends. These obligations are based on current balance sheet values and include expected interest



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crediting, but do not incorporate an expectation of future market growth, or future deposits. Due to the significance of the assumptions used, the amounts presented could materially differ from actual results. As variable separate account obligations are legally insulated from general account obligations, the variable separate account obligations will be fully funded by cash flows from variable separate account assets. We expect to fully fund the general account obligations from cash flows from general account investments.

(9) Excluded from this table are certain pension obligations.

### **FAIR VALUE OF FINANCIAL INSTRUMENTS**

FASB guidance defines fair value for GAAP and establishes a framework for measuring fair value as well as a fair value hierarchy based on the quality of inputs used to measure fair value and enhances disclosure requirements for fair value measurements. The term *fair value* in this document is defined in accordance with GAAP. The standard describes three levels of inputs that may be used to measure fair value. For more information, see Note 2, *Summary of Significant Accounting Policies* and Note 16, *Fair Value of Financial Instruments*.

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Available-for-sale securities and trading account securities are recorded at fair value, which is primarily based on actively traded markets where prices are based on either direct market quotes or observed transactions. Liquidity is a significant factor in the determination of the fair value for these securities. Market price quotes may not be readily available for some positions or for some positions within a market sector where trading activity has slowed significantly or ceased. These situations are generally triggered by the market's perception of credit uncertainty regarding a single company or a specific market sector. In these instances, fair value is determined based on limited available market information and other factors, principally from reviewing the issuer's financial position, changes in credit ratings, and cash flows on the investments. As of June 30, 2014, \$2.4 billion of available-for-sale and trading account assets, excluding other long-term investments, were classified as Level 3 fair value assets.

The fair values of derivative assets and liabilities include adjustments for market liquidity, counterparty credit quality, and other deal specific factors, where appropriate. The fair values of derivative assets and liabilities traded in the over-the-counter market are determined using quantitative models that require the use of multiple market inputs including interest rates, prices, and indices to generate continuous yield or pricing curves and volatility factors. The predominance of market inputs are actively quoted and can be validated through external sources. Estimation risk is greater for derivative financial instruments that are either option-based or have longer maturity dates where observable market inputs are less readily available or are unobservable, in which case quantitative based extrapolations of rate, price, or index scenarios are used in determining fair values. As of June 30, 2014, the Level 3 fair values of derivative assets and liabilities determined by these quantitative models were \$123.3 million and \$484.7 million, respectively.

The liabilities of certain of our annuity account balances are calculated at fair value using actuarial valuation models. These models use various observable and unobservable inputs including projected future cash flows, policyholder behavior, our credit rating, and other market conditions. As of June 30, 2014, the Level 3 fair value of these liabilities was \$102.5 million.

For securities that are priced via non-binding independent broker quotations, we assess 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. We use 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 we determine there is a more appropriate fair value based upon the analytics, the price received from the independent broker is adjusted accordingly. We did not adjust any quotes or prices received from brokers during the six months ended June 30, 2014.

Of our \$2.5 billion, or 4.7%, of total assets (measured at fair value on a recurring basis) classified as Level 3 assets, \$745.3 million were ABS. Of this amount, \$576.6 million were student loan related ABS and \$168.7 million were non-student loan related ABS. The years of issuance of the ABS are as follows:

| Year of Issuance | Amount<br>(Dollars In Millions) |       |
|------------------|---------------------------------|-------|
| 2002             | \$                              | 295.8 |
| 2003             |                                 | 98.1  |
| 2004             |                                 | 115.4 |
| 2006             |                                 | 13.0  |
| 2007             |                                 | 93.7  |
| 2012             |                                 | 104.4 |
| 2013             |                                 | 24.9  |
| Total            | \$                              | 745.3 |

The ABS was rated as follows: \$478.3 million were AAA rated, \$172.6 million were AA rated, \$91.5 million were A rated, \$2.3 million were BBB rated, and \$0.6 million were less than investment grade. We do not expect any credit losses on these securities related to student loans since the majority of the underlying collateral of the student loan asset-backed securities is guaranteed by the U.S. Department of Education.

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**MARKET RISK EXPOSURES AND OFF-BALANCE SHEET ARRANGEMENTS**

Our financial position and earnings are subject to various market risks including changes in interest rates, the yield curve, spreads between risk-adjusted and risk-free interest rates, foreign currency rates, used vehicle prices, and equity price risks and issuer defaults. We analyze and manage the risks arising from market exposures of financial instruments, as well as other risks, through an integrated asset/liability management process. Our asset/liability management programs and procedures involve the monitoring of asset and liability durations for various product lines; cash flow testing under various interest rate scenarios; and the continuous rebalancing of assets and liabilities with respect to yield, credit and market risk, and cash flow characteristics. These programs also incorporate the use of derivative financial instruments primarily to reduce our exposure to interest rate risk, inflation risk, currency exchange risk, volatility risk, and equity market risk. See Note 16, *Derivative Financial Instruments* for additional information on our financial instruments.

The primary focus of our asset/liability program is the management of interest rate risk within the insurance operations. This includes monitoring the duration of both investments and insurance liabilities to maintain an appropriate balance between risk and profitability for each product category, and for us as a whole. It is our policy to maintain asset and liability durations within one year of one another, although, from time to time, a broader interval may be allowed.

We are exposed to credit risk within our investment portfolio and through derivative counterparties. Credit risk relates to the uncertainty of an obligor's continued ability to make timely payments in accordance with the contractual terms of the instrument or contract. We manage credit risk through established investment policies which attempt to address quality of obligors and counterparties, credit concentration limits, diversification requirements, and acceptable risk levels under expected and stressed scenarios. Derivative counterparty credit risk is measured as the amount owed to us, net of collateral held, based upon current market conditions. In addition, we periodically assess exposure related to potential payment obligations between us and our counterparties. We minimize the credit risk in derivative financial instruments by entering into transactions with high quality counterparties, (A-rated or higher at the time we enter into the contract) and we maintain credit support annexes with certain of those counterparties.

We utilize a risk management strategy that includes the use of derivative financial instruments. Derivative instruments expose us to credit market and basis risk. Such instruments can change materially in value from period-to-period. We minimize our credit risk by entering into transactions with highly rated counterparties. We manage the market and basis risks by establishing and monitoring limits as to the types and degrees of risk that may be undertaken. We monitor our use of derivatives in connection with our overall asset/liability management programs and procedures. In addition, all derivative programs are monitored by our risk management department.

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

We may use the following types of derivative contracts to mitigate our exposure to certain guaranteed benefits related to variable annuity contracts and fixed indexed annuities:

- Foreign Currency Futures

- Variance Swaps
- Interest Rate Futures
- Equity Options
- Equity Futures
- Credit Derivatives
- Interest Rate Swaps
- Interest Rate Swaptions
- Volatility Futures
- Volatility Options
- Total Return Swaps

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We believe our asset/liability management programs and procedures and certain product features provide protection against the effects of changes in interest rates under various scenarios. Additionally, we believe our asset/liability management programs and procedures provide sufficient liquidity to enable us to fulfill our obligation to pay benefits under our various insurance and deposit contracts. However, our asset/liability management programs and procedures incorporate assumptions about the relationship between short-term and long-term interest rates (i.e., the slope of the yield curve), relationships between risk-adjusted and risk-free interest rates, market liquidity, spread movements, implied volatility, policyholder behavior, and other factors, and the effectiveness of our asset/liability management programs and procedures may be negatively affected whenever actual results differ from those assumptions.

In the ordinary course of our commercial mortgage lending operations, we may commit to provide a mortgage loan before the property to be mortgaged has been built or acquired. The mortgage loan commitment is a contractual obligation to fund a mortgage loan when called upon by the borrower. The commitment is not recognized in our financial statements until the commitment is actually funded. The mortgage loan commitment contains terms, including the rate of interest, which may be different than prevailing interest rates. As of June 30, 2014, we had outstanding mortgage loan commitments of \$489.6 million at an average rate of 4.84%.

**Impact of continued low interest rate environment**

Significant changes in interest rates expose us to the risk of not realizing anticipated spreads between the interest rate earned on investments and the interest rate credited to in-force policies and contracts. In addition, certain of our insurance and investment products guarantee a minimum credited interest rate ( MGIR ). In periods of prolonged low interest rates, the interest spread earned may be negatively impacted to the extent our ability to reduce policyholder crediting rates is limited by the guaranteed minimum credited interest rates. Additionally, those policies without account values may exhibit lower profitability in periods of prolonged low interest rates due to reduced investment income.

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The table below presents account values by range of current minimum guaranteed interest rates and current crediting rates for our universal life and deferred fixed annuity products:

**Credited Rate Summary**

As of June 30, 2014

| Minimum Guaranteed Interest Rate<br>Account Value | At<br>MGIR            | 1-50 bps<br>above<br>MGIR | More than<br>50 bps<br>above MGIR | Total     |
|---|-----------------------|---------------------------|-----------------------------------|-----------|
|   | (Dollars In Millions) |                           |                                   |           |
| <b>Universal Life Insurance</b>                   |                       |                           |                                   |           |
| >2% - 3%  | \$ 184                | \$ 928                    | \$ 1,998                          | \$ 3,110  |
| >3% - 4%  | 3,531                 | 1,677                     | 136                               | 5,344     |
| >4% - 5%  | 2,069                 | 15                        |                                   | 2,084     |
| >5% - 6%  | 227                   |                           |                                   | 227       |
| Subtotal  | 6,011                 | 2,620                     | 2,134                             | 10,765    |
| <b>Fixed Annuities</b>                            |                       |                           |                                   |           |
| 1%  | \$ 530                | \$ 191                    | \$ 323                            | \$ 1,044  |
| >1% - 2%  | 603                   | 527                       | 221                               | 1,351     |
| >2% - 3%  | 1,992                 | 115                       | 589                               | 2,696     |
| >3% - 4%  | 300                   |                           |                                   | 300       |
| >4% - 5%  | 304                   |                           |                                   | 304       |
| Subtotal  | 3,729                 | 833                       | 1,133                             | 5,695     |
| Total   | \$ 9,740              | \$ 3,453                  | \$ 3,267                          | \$ 16,460 |
| Percentage of Total                               | 59%                   | 21%                       | 20%                               | 100%      |

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The table below presents account values by range of current minimum guaranteed interest rates and current crediting rates for our universal life and deferred fixed annuity products:

**Credited Rate Summary****As of December 31, 2013**

| Minimum Guaranteed Interest Rate<br>Account Value | At<br>MGIR | 1-50 bps<br>above<br>MGIR | More than<br>50 bps<br>above MGIR | Total     |
|---|------------|---------------------------|-----------------------------------|-----------|
| (Dollars In Millions)                             |            |                           |                                   |           |
| <b>Universal Life Insurance</b>                   |            |                           |                                   |           |
| >2% - 3%  | \$ 43      | \$ 1,024                  | \$ 1,984                          | \$ 3,051  |
| >3% - 4%  | 3,109      | 2,099                     | 150                               | 5,358     |
| >4% - 5%  | 2,110      | 15                        |                                   | 2,125     |
| >5% - 6%  | 232        |                           |                                   | 232       |
| Subtotal  | 5,494      | 3,138                     | 2,134                             | 10,766    |
| <b>Fixed Annuities</b>                            |            |                           |                                   |           |
| 1%  | \$ 422     | \$ 173                    | \$ 461                            | \$ 1,056  |
| >1% - 2%  | 612        | 518                       | 279                               | 1,409     |
| >2% - 3%  | 1,846      | 308                       | 632                               | 2,786     |
| >3% - 4%  | 309        |                           |                                   | 309       |
| >4% - 5%  | 313        |                           |                                   | 313       |
| Subtotal  | 3,502      | 999                       | 1,372                             | 5,873     |
| Total   | \$ 8,996   | \$ 4,137                  | \$ 3,506                          | \$ 16,639 |
| Percentage of Total                               | 54%        | 25%                       | 21%                               | 100%      |

We are active in mitigating the impact of a continued low interest rate environment through product design, as well as adjusting crediting rates on current in-force policies and contracts. We also manage interest rate and reinvestment risks through our asset/liability management process. Our asset/liability management programs and procedures involve the monitoring of asset and liability durations; cash flow testing under various interest rate scenarios; and the regular rebalancing of assets and liabilities with respect to yield, credit and market risk, and cash flow characteristics. These programs also incorporate the use of derivative financial instruments primarily to reduce our exposure to interest rate risk, inflation risk, currency exchange risk, volatility risk, and equity market risk.

**IMPACT OF INFLATION**

Inflation increases the need for life insurance. Many policyholders who once had adequate insurance programs may increase their life insurance coverage to provide the same relative financial benefit and protection. Higher interest rates may result in higher sales of certain of our investment products.



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The higher interest rates that have traditionally accompanied inflation could also affect our operations. Policy loans increase as policy loan interest rates become relatively more attractive. As interest rates increase, disintermediation of stable value and annuity account balances and individual life policy cash values may increase. The market value of our fixed-rate, long-term investments may decrease, we may be unable to implement fully the interest rate reset and call provisions of our mortgage loans, and our ability to make attractive mortgage loans, including participating mortgage loans, may decrease. In addition, participating mortgage loan income may decrease. The difference between the interest rate earned on investments and the interest rate credited to life insurance and investment products may also be adversely affected by rising interest rates.

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**RECENTLY ISSUED ACCOUNTING STANDARDS**

See Note 2, *Summary of Significant Accounting Policies*, to the consolidated condensed financial statements for information regarding recently issued accounting standards.

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

See Part I, Item 2, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, Executive Summary and Liquidity and Capital Resources, and Part II, Item 1A, *Risk Factors and Cautionary Factors that may Affect Future Results*, of this report for market risk disclosures.

**Item 4. Controls and Procedures**

**(a) Disclosure controls and procedures**

In order to ensure that the information the Company must disclose in its filings with the Securities and Exchange Commission is recorded, processed, summarized, and reported on a timely basis, the Company's management, with the participation of its Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), except as otherwise noted below. Based on their evaluation as of the end of the period covered by this Form 10-Q, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective. It should be noted that any system of controls, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of any control system is based in part upon certain judgments, including the costs and benefits of controls and the likelihood of future events. Because of these and other inherent limitations of control systems, no evaluation of controls can provide absolute assurance that all control issues, if any, within the Company have been detected.

In conducting our evaluation of the effectiveness of internal control over financial reporting as of June 30, 2014, the Company has excluded the internal controls relating to the administrative systems and processes being provided by third parties for MONY Life Insurance Company (MONY) and the blocks of life and health business reinsured from MONY Life Insurance Company of America (MLOA Business). As of June 30, 2014, the Company is in the process of, but has not completed its own evaluation of the design and operation of the internal controls relating to the administrative systems and processes, including those currently being provided by third parties, for MONY and the MLOA business. For the three and six months ended June 30, 2014, MONY and the MLOA Business represented revenues and pre-tax income of \$204.4 million and \$29.2 million and \$394.0 million and \$52.6 million, respectively, of the Company's consolidated income before income tax.

**(b) Changes in internal control over financial reporting**

During the three months ended June 30, 2014, the Company began the conversion and integration of administrative processing into its internal controls over financial reporting for the MONY and MLOA blocks of business.

There have been no changes in the Company's internal control over financial reporting during the six months ended June 30, 2014, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting. The Company's internal controls exist within a dynamic environment and the Company continually strives to improve its internal controls and procedures to enhance the quality of its financial reporting.

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**PART II**

**Item 1. Legal Proceedings**

Since the entry into the Merger Agreement on June 3, 2014, four lawsuits have been filed against the Company, our directors, Dai-ichi and DL Investment (Delaware), Inc. on behalf of alleged Company shareowners. On June 11, 2014, a putative class action lawsuit styled *Edelman, et al. v. Protective Life Corporation, et al.*, Civil Action No. 01-CV-2014-902474.00, was filed in the Circuit Court of Jefferson County, Alabama. On July 30, 2014, the plaintiff in *Edelman* filed an amended complaint. Three putative class action lawsuits have been filed in the Court of Chancery of the State of Delaware, including *Martin, et al. v. Protective Life Corporation, et al.*, Civil Action No. 9794-CB, filed June 19, 2014, *Leyendecker, et al. v. Protective Life Corporation, et al.*, Civil Action No. 9931-CB, filed July 22, 2014 and *Hilburn, et al. v. Protective Life Corporation, et al.*, Civil Action No. 9937-CB, filed July 23, 2014. The Delaware Court of Chancery consolidated the *Martin, Leyendecker* and *Hilburn* actions under the caption *In re Protective Life Corp. Stockholders Litigation*, Consolidated Civil Action No. 9794-CB, designated the *Hilburn* complaint as the operative consolidated complaint and appointed Charlotte Martin, Samuel J. Leyendecker, Jr., and Deborah J. Hilburn to serve as co-lead plaintiffs. These lawsuits allege that our Board of Directors breached its fiduciary duties to our shareowners, that the Merger involves an unfair price, an inadequate sales process, and unreasonable deal protection devices that purportedly preclude competing offers, and that the preliminary proxy statement filed with the SEC on July 10, 2014 fails to disclose purportedly material information. The complaints also allege that the Company, Dai-ichi and DL Investment (Delaware), Inc. aided and abetted those alleged breaches of fiduciary duties. The complaints seek injunctive relief, including enjoining or rescinding the Merger, and attorneys' and other fees and costs, in addition to other relief. The consolidated Delaware action also seeks an award of unspecified damages. The Company and our Board of Directors believe these claims are without merit and intend to vigorously defend these actions. We cannot predict the outcome of or estimate the possible loss or range of loss from these matters.

Except as set forth above, to the knowledge and in the opinion of management, there are no material pending legal proceedings, other than ordinary routine litigation incidental to the business of the Company, to which the Company or any of its subsidiaries is a party or of which any of our properties is the subject. For additional information regarding legal proceedings, see Part II, Item 1A, *Risk Factors and Cautionary Factors that may Affect Future Results*, of this report and Note 10, *Commitments and Contingencies*, to the consolidated condensed financial statements.

**Item 1A. Risk Factors and Cautionary Factors that may Affect Future Results**

The operating results of companies in the insurance industry have historically been subject to significant fluctuations. The factors which could affect the Company's future results include, but are not limited to, general economic conditions and known trends and uncertainties. In addition to other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A, *Risk Factors and Cautionary Factors that may Affect Future Results* in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, and the factors discussed in Part II, Item 1A, *Risk Factors and Cautionary Factors that may Affect Future Results* in the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2014, which could materially affect the Company's business, financial condition, or future results of operations.

**Risks Related to the Proposed Dai-ichi Merger**

*The Merger is subject to various closing conditions, including regulatory and third party approvals.*

As discussed above, on June 3, 2014, the Company entered into the Merger Agreement pursuant to which it would become a wholly owned subsidiary of Dai-ichi. Completion of the Merger is subject to certain closing conditions, including, without limitation, approval of the Company's shareowners, the receipt of required third party consents and regulatory approvals, including those of the Financial Services Agency of Japan and domestic insurance regulators, the expiration or termination of the applicable waiting period under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, which waiting period terminated on July 25, 2014, pursuant to a grant of early termination by the Federal Trade Commission, the absence of legal impediments or a material adverse effect with respect to the Company preventing the consummation of the Merger, as well as other conditions to closing as are customary in transactions such as the Merger. A number of the closing conditions are outside of our control and we cannot predict with certainty whether all of the required closing conditions will be satisfied or waived or if other uncertainties may arise. In addition, regulators could impose additional requirements or obligations as conditions for their approvals, which may be burdensome. Despite our best efforts, we

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may not be able to satisfy the various closing conditions or obtain the necessary waivers or approvals in a timely fashion or at all, in which case the Merger would be prevented or delayed.

***Failure to timely complete the Merger could adversely impact our stock price, business, financial condition and results of operations.***

There is no assurance that the conditions to the Merger will be satisfied in a timely manner, or that the Merger will occur. A failure to consummate the Merger on a timely basis or at all could result in negative publicity and cause the price of our common stock to decline, to the extent our current stock price reflects a market assumption that the Merger will occur. In addition, as a result of the announcement of the Merger Agreement, trading in our stock has increased substantially. If the Merger is not consummated, the investment goals of our shareowners may be materially different than those of our shareowners on a pre-Merger announcement basis. In addition, we will remain liable for significant transaction costs that will be payable even if the Merger is not completed and could also be required to pay a termination fee to Dai-ichi in certain specific circumstances. For these and other reasons, failure to timely consummate the Merger could adversely impact our stock price and perceived acquisition value, business, financial condition and results of operations.

***The pendency of the Merger and operating restrictions contained in the Merger Agreement could adversely affect our business and operations.***

The proposed Merger could cause disruptions to the Company's business and business relationships, which could have an adverse impact on the Company's results of operations, liquidity and financial condition. For example, the attention of the Company's management may be directed to Merger related considerations, the Company's current and prospective employees may experience uncertainty about their future roles with the Company which may adversely affect our ability to retain and hire key personnel, and parties with which the Company has business relationships, including customers, potential customers and distributors, may experience uncertainty as to the future of such relationships and seek alternative relationships with third parties or seek to alter their present business relationships with us in a manner that negatively impacts the Company. In addition, the Company has incurred, and will continue to incur, significant transaction costs in connection with the Merger, and many of these fees and costs are payable regardless of whether the Merger is consummated.

***Shareowner litigation against the Company, our directors and/or Dai-ichi could delay or prevent the Merger and cause us to incur significant costs and expenses.***

Transactions such as the Merger are often subject to lawsuits by shareowners. To date, multiple purported class action lawsuits have been filed by shareowners seeking injunctive relief, including enjoining or rescinding the Merger, an award of unspecified damages, attorneys' and other fees and costs, and other relief. Conditions to the closing of the Merger require that no laws or legal restraints must have been adopted or in effect, and that no restraining order, injunction or other order, judgment, decision, opinion or decree must have been issued, in each case having the effect of making the Merger illegal or otherwise prohibiting the consummation of the Merger. We cannot assure you as to the outcome of these or any similar future lawsuits, including the costs associated with defending the claims or any other liabilities that may be incurred in connection with the litigation or settlement of these lawsuits. If the plaintiffs are successful in obtaining an injunction prohibiting the parties from completing the Merger on the agreed-upon terms, such an injunction may prevent the completion of the Merger in the expected time frame or altogether.

***Our debt ratings and the financial strength ratings of our insurance subsidiaries may be adversely affected by the transactions contemplated by the Merger Agreement.***

Following the announcement of the Dai-ichi transaction, the rating agencies have undertaken a review of our debt ratings and our insurance company subsidiaries' financial strength ratings. See Item 2, *Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources - Ratings*, for additional information regarding the rating agencies and our ratings. The rating agencies may take various actions, positive or negative, and the result may not be known until the Merger closes. Any negative action by a ratings agency could have a material adverse impact on the Company's financial condition or results of operations.

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**General Risk Factors**

*The Company may not realize its anticipated financial results from its acquisitions strategy.*

The Company's acquisitions of companies and acquisitions or coinsurance of blocks of insurance business have increased its earnings in part by allowing the Company to position itself to realize certain operating efficiencies. However, there can be no assurance that the Company will have future suitable opportunities for, or sufficient capital available to fund, such transactions. If our competitors have access to capital on more favorable terms or at a lower cost, our ability to compete for acquisitions may be diminished. In addition, there can be no assurance that the Company will realize the anticipated financial results from such transactions.

The Company may be unable to complete an acquisition transaction. Completion of an acquisition transaction may be more costly or take longer than expected, or may have a different or more costly financing structure than initially contemplated. In addition, the Company may not be able to complete or manage multiple acquisition transactions at the same time, or the completion of such transactions may be delayed or be more costly than initially contemplated. The Company or other parties to the transaction may be unable to obtain regulatory approvals required to complete an acquisition transaction. If the Company identifies and completes suitable acquisitions, it may not be able to successfully integrate the business in a timely or cost-effective manner. In addition, there may be unforeseen liabilities that arise in connection with businesses or blocks of insurance business that the Company acquires.

Additionally, in connection with its acquisition transactions that involve reinsurance, the Company assumes, or otherwise becomes responsible for, the obligations of policies and other liabilities of other insurers. Any regulatory, legal, financial, or other adverse development affecting the other insurer could also have an adverse effect on the Company.

**Risks Related to the Financial Environment**

*The Company's investments are subject to market and credit risks. These risks could be heightened during periods of extreme volatility or disruption in financial and credit markets.*

The Company's invested assets and derivative financial instruments are subject to risks of credit defaults and changes in market values. These risks could be heightened during periods of extreme volatility or disruption in the financial and credit markets, including as a result of social or political unrest or instability domestically or abroad. A widening of credit spreads will increase the unrealized losses in the Company's investment portfolio. The factors affecting the financial and credit markets could lead to other-than-temporary impairments of assets in the Company's investment portfolio.

The value of the Company's commercial mortgage loan portfolio depends in part on the financial condition of the tenants occupying the properties that the Company has financed. The value of the Company's investment portfolio, including its portfolio of government debt obligations, debt obligations of those entities with an express or implied governmental guarantee and debt obligations of other issuers holding a large amount of such obligations, depends in part on the ability of the issuers or guarantors of such debt to maintain their credit ratings and meet



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their contractual obligations. Factors that may affect the overall default rate on, and market value of, the Company's invested assets, derivative financial instruments, and mortgage loans include interest rate levels, financial market performance, and general economic conditions as well as particular circumstances affecting the individual tenants, borrowers, issuers and guarantors.

Significant continued financial and credit market volatility, changes in interest rates and credit spreads, credit defaults, real estate values, market illiquidity, declines in equity prices, acts of corporate malfeasance, ratings downgrades of the issuers or guarantors of these investments, and declines in general economic conditions, either alone or in combination, could have a material adverse impact on the Company's results of operations, financial condition, or cash flows through realized losses, impairments, changes in unrealized loss positions, and increased demands on capital, including obligations to post additional capital and collateral. In addition, market volatility can make it difficult for the Company to value certain of its assets, especially if trading becomes less frequent. Valuations may include assumptions or estimates that may have significant period-to-period changes that could have an adverse impact on the Company's results of operations or financial condition.

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***Credit market volatility or disruption could adversely impact the Company's financial condition or results from operations.***

Significant volatility or disruption in domestic or foreign credit markets, including as a result of social or political unrest or instability, could have an adverse impact in several ways on either the Company's financial condition or results from operations. Changes in interest rates and credit spreads could cause market price and cash flow variability in the fixed income instruments in the Company's investment portfolio. Significant volatility and lack of liquidity in the credit markets could cause issuers of the fixed-income securities in the Company's investment portfolio to default on either principal or interest payments on these securities. Additionally, market price valuations may not accurately reflect the underlying expected cash flows of securities within the Company's investment portfolio.

The Company's statutory surplus is also impacted by widening credit spreads as a result of the accounting for the assets and liabilities on its fixed market value adjusted ( MVA ) annuities. Statutory separate account assets supporting the fixed MVA annuities are recorded at fair value. In determining the statutory reserve for the fixed MVA annuities, the Company is required to use current crediting rates based on U.S. Treasuries. In many capital market scenarios, current crediting rates based on U.S. Treasuries are highly correlated with market rates implicit in the fair value of statutory separate account assets. As a result, the change in the statutory reserve from period to period will likely substantially offset the change in the fair value of the statutory separate account assets. However, in periods of volatile credit markets, actual credit spreads on investment assets may increase sharply for certain sub-sectors of the overall credit market, resulting in statutory separate account asset market value losses. Credit spreads are not consistently fully reflected in crediting rates based on U.S. Treasuries, and the calculation of statutory reserves will not substantially offset the change in fair value of the statutory separate account assets resulting in reductions in statutory surplus. This situation would result in the need to devote significant additional capital to support fixed MVA annuity products.

Volatility or disruption in the credit markets could also impact the Company's ability to efficiently access financial solutions for purposes of issuing long-term debt for financing purposes, its ability to obtain financial solutions for purposes of supporting certain traditional and universal life insurance products for capital management purposes, or result in an increase in the cost of existing securitization structures.

The ability of the Company to implement financing solutions designed to fund a portion of statutory reserves on both the traditional and universal life blocks of business is dependent upon factors such as the ratings of the Company, the size of the blocks of business affected, the mortality experience of the Company, the credit markets, and other factors. The Company cannot predict the continued availability of such solutions or the form that the market may dictate. To the extent that such financing solutions were desired but are not available, the Company's financial position could be adversely affected through impacts including, but not limited to, higher borrowing costs, surplus strain, lower sales capacity, and possible reduced earnings expectations.

***The Company could be adversely affected by an inability to access FHLB lending.***

During the fourth quarter of 2010, the Federal Housing Finance Agency ( FHFA ) issued an Announced Notice of Proposed Rulemaking ( ANPR ). The purpose of the ANPR is to seek comment on several possible changes to the requirements applicable to members of the Federal Home Loan Bank ( FHLB ). Any changes to such requirements that eliminate the Company's eligibility for continued FHLB membership or limit the Company's borrowing capacity pursuant to its FHLB membership could have a material adverse effect on the Company. The Company can give no assurance as to the outcome of the ANPR. The FHFA also released an advisory bulletin on the particular risks associated with lending to insurance companies as opposed to federally-backed banks, which includes standards for evaluating FHLB's lending to an insurance company member. These standards are broad and raise concerns about the state regulatory framework and of FHLB creditor status in the event of insurer insolvency. In March 2013, the FHFA issued a report entitled FHFA Can Enhance Its Oversight of FHLBank Advances to Insurance Companies by Improving Communication with State Insurance Regulators and Industry Groups, which proposes the FHFA coordinate with state regulators

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to obtain confidential supervisory information about insurers and interact with NAIC working groups to receive early warning information about failing members, so the FHFA can participate in the rehabilitation and perhaps increase FHLB creditor status. Pursuant to these recommendations, individual FHLB members worked with the NAIC and trade groups on model legislation that would enable insurers to access FHLB funding on similar collateral terms as federally insured depository institutions. The FHLB members were not able to

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obtain significant agreement with NAIC membership on several points; however, legislation based on the model has been introduced in several states and is not being opposed by the NAIC. Any standards or events that result in stricter regulation of or a reduced incidence of FHLB-insurer lending could have a material adverse effect on the Company.

**Industry Related Risks**

*The business of the Company is highly regulated and is subject to routine audits, examinations and actions by regulators, law enforcement agencies and self-regulatory organizations.*

The Company is subject to government regulation in each of the states in which it conducts business. In many instances, the regulatory models emanate from the National Association of Insurance Commissioners ( NAIC ). Such regulation is vested in state agencies having broad administrative and in some instances discretionary power dealing with many aspects of the Company s business, which may include, among other things, premium rates and increases thereto, underwriting practices, reserve requirements, marketing practices, advertising, privacy, policy forms, reinsurance reserve requirements, insurer use of captive reinsurance companies, acquisitions, mergers, capital adequacy, claims practices and the remittance of unclaimed property. In addition, some state insurance departments may enact rules or regulations with extra-territorial application, effectively extending their jurisdiction to areas such as permitted insurance company investments that are normally the province of an insurance company s domiciliary state regulator.

At any given time, a number of financial, market conduct, or other examinations or audits of the Company s subsidiaries may be ongoing. It is possible that any examination or audit may result in payments of fines and penalties, payments to customers, or both, as well as changes in systems or procedures, any of which could have a material adverse effect on the Company s financial condition or results of operations.

The Company s insurance subsidiaries are required to obtain state regulatory approval for rate increases for certain health insurance products. The Company s profits may be adversely affected if the requested rate increases are not approved in full by regulators in a timely fashion.

State insurance regulators and the NAIC regularly re-examine existing laws and regulations applicable to insurance companies and their products. Changes in these laws and regulations, or in interpretations thereof, are often made for the benefit of the consumer and may lead to additional expense for the insurer and, thus, could have a material adverse effect on the Company s financial condition and results of operations. The NAIC may also be influenced by the initiatives and regulatory structures or schemes of international regulatory bodies, and those initiatives or regulatory structures or schemes may not translate readily into the regulatory structures or schemes or the legal system (including the interpretation or application of standards by juries) under which U.S. insurers must operate. In August 2013, the Financial Stability Board ( FSB ) released a report encouraging the U.S. to move toward a federal regulatory system for insurance. The International Association of Insurance Supervisors ( IAIS ) is developing group-wide supervision requirements, including a global capital standard, to be applied to large, internationally active insurance groups ( IAIGs ), as well as standards for companies posing systemic risk to be applied to global systemically important insurers ( G-SII s ). These are only a few examples of international developments impacting the global insurance market. At this time, FSB reports, IAIS Insurance Core Principles, and other international work products are not directly binding on the Company, and the Company has not been identified as either an IAIG or G-SII. However, there is increasing pressure to conform to international standards due to the globalization of the business of insurance and the recent financial crisis. Any international reports or mandates that directly impact, or indirectly influence, the nature of U.S. regulation or industry operations could impact the Company.

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Although some NAIC pronouncements, particularly as they affect accounting, reserving and risk based capital issues, may take effect automatically without affirmative action taken by the states, the NAIC is not a governmental entity and its processes and procedures do not comport with those to which governmental entities typically adhere. Therefore, it is possible that actions could be taken by the NAIC that become effective without the procedural safeguards that would be present if governmental action was required. In addition, with respect to some financial regulations and guidelines, states sometimes defer to the interpretation of the insurance department of a non-domiciliary state. Neither the action of the domiciliary state nor the action of the NAIC is binding on a state. Accordingly, a state could choose to follow a different interpretation. The Company is also subject to the risk that compliance with any particular regulator's interpretation of a legal, accounting or actuarial issue may result in non-compliance with another

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regulator's interpretation of the same issue, particularly when compliance is judged in hindsight. There is an additional risk that any particular regulator's interpretation of a legal, accounting or actuarial issue may change over time to the Company's detriment, or that changes to the overall legal or market environment may cause the Company to change its practices in ways that may, in some cases, limit its growth or profitability. Statutes, regulations, interpretations, and instructions may be applied with retroactive impact, particularly in areas such as accounting, reserve and risk based capital requirements. Also, regulatory actions with prospective impact can potentially have a significant impact on currently sold products.

The NAIC has announced more focused inquiries on certain matters that could have an impact on the Company's financial condition and results of operations. Such inquiries concern, for example, examination of statutory accounting disclosures for separate accounts, insurer use of captive reinsurance companies, certain aspects of insurance holding company reporting and disclosure, reserving for universal life products with secondary guarantees, reinsurance, and risk based capital calculations. In addition, the NAIC continues to consider various initiatives to change and modernize its financial and solvency requirements and regulations. It is considering changing to, or has considered and passed, a principles-based reserving method for life insurance and annuity reserves, changes to the accounting and risk-based capital regulations, changes to the governance practices of insurers, and other items. Some of these proposed changes, including implementing a principles-based reserving methodology, would require the approval of state legislatures. The Company cannot provide any estimate as to what impact these more focused inquiries or proposed changes, if they occur, will have on its product mix, product profitability, reserve and capital requirements, financial condition or results of operations.

With respect to reserving requirements for universal life policies with secondary guarantees ( ULSG ), in 2012 the NAIC adopted revisions to Actuarial Guideline XXXVIII ( AG38 ) addressing those requirements. Some of the regulatory participants in the AG38 revision process appeared to believe that one of the purposes of the revisions was to calculate reserves for ULSG similarly to reserves for guaranteed level term life insurance contracts with the same guarantee period. The effect of the revisions was to increase the level of reserves that must be held by insurers on ULSG with certain product designs that are issued on and after January 1, 2013, and to cause insurers to test the adequacy of reserves, and possibly increase the reserves, on ULSG with certain product designs that were issued before January 1, 2013. The Company has developed and introduced a new ULSG product for sales in 2013. The Company cannot predict future regulatory actions that could negatively impact the Company's ability to market its new product. Such regulatory reactions could include, for example, withdrawal of state approvals of the new product, or adoption of further changes to AG38 or other adverse action including retroactive regulatory action that could negatively impact the Company's new product. A disruption of the Company's ability to sell financially viable life insurance products or an increase in reserves on ULSG policies issued either before or after January 1, 2013, could have a material adverse impact on the Company's financial condition or results of operations.

The Company currently uses affiliated captive reinsurance companies in various structures relating to term life insurance and universal life insurance with secondary guarantees, and certain guaranteed benefits relating to variable annuities, to finance statutory requirements for so-called XXX and AXXX reserves and reserves for variable annuity contracts with guaranteed minimum withdrawal and death benefits. The NAIC, through various committees, subgroups and dedicated task forces, has undertaken a review of the use of captives and special purpose vehicles used to transfer insurance risk in relation to existing state laws and regulations, and several committees have adopted or exposed for comment white papers and reports that, if or when implemented, place significant limitations on the use of captives and other reinsurers (including traditional reinsurers) (the Affected Business ). The NAIC's Financial Condition (E) Committee adopted an interim solution for captives in the form of a new charge requiring the Financial Analysis Working Group (or FAWG ) to review captive transactions submitted by the states in a peer review and comment process. The Principles Based Reserving Implementation (EX) Task Force of the NAIC, charged with analysis of the adoption of a principles-based reserving methodology, recently adopted the conceptual framework contained in a report issued by Rector & Associates, Inc., dated June 4, 2014 (as modified or supplemented, the Rector Report ), that contains numerous recommendations pertaining to the regulation and use of captive reinsurers. At this time, certain high-level recommendations have been adopted and are being assigned to various NAIC working groups. However, the recommendations in the Rector Report are subject to ongoing comment and revision. It is unclear at this time whether or to what extent the recommendations in the Rector Report, or additional or revised recommendations relating to captive transactions or reinsurance transactions in general, will be adopted by the NAIC. If the recommendations proposed in the Rector Report are implemented, it will likely be difficult for the Company to establish new captive



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financing arrangements on a basis consistent with past practices and in some circumstances could impact the Company's ability to engage in certain reinsurance transactions with non-affiliates.

The NAIC's Financial Regulation Standards and Accreditation (F) Committee is considering a proposal to include insurer-owned captives and special purpose vehicles that are single-state licensed but assume reinsurance from cedants operating in multiple states within the definition of "multi-state insurer" found in the preambles to Parts A and B of the NAIC Financial Regulation Standards and Accreditation Program. If adopted, the revised definition would subject captives (on a prospective basis, as proposed) to all of the Accreditation Standards applicable to other traditional multi-state insurers, including standards related to capital and surplus requirements, risk-based capital requirements, investment laws and credit for reinsurance laws. Such application would likely have a significant and adverse impact on the Company's ability to engage in captive finance transactions on the same or a similar basis as in past periods.

Any regulatory action or changes in interpretation that materially adversely affects the Company's use or materially increases the Company's cost of using captives or reinsurers for the Affected Business, either retroactively or prospectively, could have a material adverse impact on the Company's financial condition or results of operations. If the Company were required to discontinue its use of captives for intercompany reinsurance transactions on a retroactive basis, adverse impacts would include early termination fees payable with respect to certain structures, diminished capital position and higher cost of capital. Additionally, finding alternative means to support policy liabilities efficiently is an unknown factor that would be dependent, in part, on future market conditions and the Company's ability to obtain required regulatory approvals. On a prospective basis, discontinuation of the use of captives could impact the types, amounts and pricing of products offered by the Company's insurance subsidiaries.

Recently, new laws and regulations have been adopted in certain states that require life insurers to search for unreported deaths. The National Conference of Insurance Legislators (NCOIL) has adopted the Model Unclaimed Life Insurance Benefits Act (the "Unclaimed Benefits Act") and legislation has been enacted in various states that is similar to the Unclaimed Benefits Act, although each state's version differs in some respects. The Unclaimed Benefits Act would impose new requirements on insurers to periodically compare their in-force life insurance and annuity contracts and retained asset accounts against a Death Database, investigate any potential matches to confirm the death and determine whether benefits are due, and to attempt to locate the beneficiaries of any benefits that are due or, if no beneficiary can be located, escheat the benefit to the state as unclaimed property. Other states in which the Company does business may also consider adopting legislation similar to the Unclaimed Benefits Act. The Company cannot predict whether such legislation will be proposed or enacted in additional states. The NAIC recently formed an Unclaimed Life Insurance Benefits (A) Working Group to study whether the NAIC should make recommendations pertaining to unclaimed life benefits. Other life insurance industry associations and regulatory associations are also considering these matters.

A number of state treasury departments and administrators of unclaimed property have audited life insurance companies for compliance with unclaimed property laws. The focus of the audits has been to determine whether there have been maturities of policies or contracts, or policies that have exceeded limiting age with respect to which death benefits or other payments under the policies should be treated as unclaimed property that should be escheated to the state. In addition, the audits have sought to identify unreported deaths of insureds. There is no clear basis in previously existing law for treating an unreported death as giving rise to a policy benefit that would be subject to unclaimed property procedures. A number of life insurers, however, have entered into resolution agreements with state treasury departments under which the life insurers agreed to procedures for comparing their previously issued life insurance and annuity contracts and retained asset accounts against a Death Database, treating confirmed deaths as giving rise to a death benefit under their policies, locating beneficiaries and paying them the benefits and interest, and escheating the benefits and interest to the state if the beneficiary could not be found. The amounts publicly reported to have been paid to beneficiaries and/or escheated to the states have been substantial.

The NAIC has established an Investigations of Life/Annuity Claims Settlement Practices (D) Task Force to coordinate targeted multi-state examinations of life insurance companies on claims settlement practices. The state insurance regulators on the Task Force have initiated targeted



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multi-state examinations of life insurance companies with respect to the companies' claims paying practices and use of a Death Database to identify unreported deaths in their life insurance policies, annuity contracts and retained asset accounts. There is no clear basis in previously existing law for requiring a life insurer to search for unreported deaths in order to determine whether a benefit is owed. A number of life insurers, however, have entered into settlement or consent agreements with state insurance regulators under which the

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life insurers agreed to implement systems and procedures for periodically comparing their life insurance and annuity contracts and retained asset accounts against a Death Database, treating confirmed deaths as giving rise to a death benefit under their policies, locating beneficiaries and paying them the benefits and interest, and escheating the benefits and interest to the state if the beneficiary could not be found. It has been publicly reported that the life insurers have paid substantial administrative and/or examination fees to the insurance regulators in connection with the settlement or consent agreements.

Certain of the Company's subsidiaries as well as certain other insurance companies from whom the Company has coinsured blocks of life insurance and annuity policies are subject to unclaimed property audits and/or targeted multistate examinations by insurance regulators similar to those described above. It is possible that the audits, examinations and/or the enactment of state laws similar to the Unclaimed Benefits Act could result in additional payments to beneficiaries, additional escheatment of funds deemed abandoned under state laws, payment of administrative penalties and/or examination fees to state authorities, and changes to the Company's procedures for identifying unreported deaths and escheatment of abandoned property. It is possible any such additional payments and any costs related to changes in Company procedures could materially impact the Company's financial results from operations. It is also possible that life insurers, including the Company, may be subject to claims, regulatory actions, law enforcement actions, and civil litigation arising from their prior business practices. Any resulting liabilities, payments or costs, including initial and ongoing costs of changes to the Company's procedures or systems, could be significant and could have a material adverse effect on the Company's financial condition or results of operations.

During December 2012, the West Virginia Treasurer filed actions against the Company's subsidiaries Protective Life Insurance Company and West Coast Life Insurance Company in West Virginia state court (*State of West Virginia ex rel. John D. Perdue vs. Protective Life Insurance Company, State of West Virginia ex rel. John D. Perdue vs. West Coast Life Insurance Company; Defendants' Motions to Dismiss granted on December 27, 2013; Notice of Appeal filed on January 27, 2014*). The actions, which also name numerous other life insurance companies, allege that the companies violated the West Virginia Uniform Unclaimed Property Act, seek to compel compliance with the Act, and seek payment of unclaimed property, interest, and penalties. While the legal theory or theories that may give rise to liability in the West Virginia Treasurer litigation are uncertain, it is possible that other jurisdictions may pursue similar actions. The Company does not currently believe that losses, if any, arising from the West Virginia Treasurer litigation will be material. The Company cannot, however, predict whether other jurisdictions will pursue similar actions or, if they do, whether such actions will have a material impact on the Company's financial results from operations. Additionally, the California Controller has recently sued several insurance carriers for alleged failure to comply with audit requests from an appointed third party auditor. The Company cannot predict whether California might pursue a similar action against the Company and further cannot predict whether other jurisdictions might pursue similar actions. The Company does not believe however that any such action would have a material impact on the Company's financial condition or results of operations.

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. From time to time, companies may be asked to contribute amounts beyond prescribed limits. The Company cannot predict the amount or timing of any future assessments.

The purchase of life insurance products is limited by state insurable interest laws, which in most jurisdictions require that the purchaser of life insurance name a beneficiary that has some interest in the sustained life of the insured. To some extent, the insurable interest laws present a barrier to the life settlement, or "stranger-owned" industry, in which a financial entity acquires an interest in life insurance proceeds, and efforts have been made in some states to liberalize the insurable interest laws. To the extent these laws are relaxed, the Company's lapse assumptions may prove to be incorrect.

At the federal level, bills are routinely introduced in both chambers of the United States Congress (Congress) that could affect life insurers. In the past, Congress has considered legislation that would impact insurance companies in numerous ways, such as providing for an optional federal charter or a federal presence for insurance, preempting state law in certain respects regarding the regulation of reinsurance, increasing

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federal oversight in areas such as consumer protection and other matters. The Company cannot predict whether or in what form legislation will be enacted and, if so, whether the enacted legislation will positively or negatively affect the Company or whether any effects will be material.

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The Company is subject to various conditions and requirements of the Healthcare Act. The Healthcare Act makes significant changes to the regulation of health insurance and may affect the Company in various ways. The Healthcare Act may affect the small blocks of business the Company has offered or acquired over the years that are, or are deemed to constitute, health insurance. The Healthcare Act may also affect the benefit plans the Company sponsors for employees or retirees and their dependents, the Company's expense to provide such benefits, the tax liabilities of the Company in connection with the provision of such benefits, and the Company's ability to attract or retain employees. In addition, the Company may be subject to regulations, guidance or determinations emanating from the various regulatory authorities authorized under the Healthcare Act. The Company cannot predict the effect that the Healthcare Act, or any regulatory pronouncement made thereunder, will have on its results of operations or financial condition.

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) enacted in July 2010 made sweeping changes to the regulation of financial services entities, products and markets. Certain provisions of Dodd-Frank are or may become applicable to the Company, its competitors or those entities with which the Company does business. Such provisions include, but are not limited to the following: the establishment of the Federal Insurance Office, changes to the regulation and standards applicable to broker-dealers and investment advisors, changes to the regulation of reinsurance, changes to regulations affecting the rights of shareowners, and the imposition of additional regulation over credit rating agencies.

Dodd-Frank also created the Financial Stability Oversight Council (the FSOC), which has issued a final rule and interpretive guidance setting forth the methodology by which it will determine whether a non-bank financial company is a systemically important financial institution (SIFI). A non-bank financial company, such as the Company, that is designated as a SIFI by the FSOC will become subject to supervision by the Board of Governors of the Federal Reserve System (the Federal Reserve). The Company is not currently supervised by the Federal Reserve. Such supervision could impact the Company's requirements relating to capital, liquidity, stress testing, limits on counterparty credit exposure, compliance and governance, early remediation in the event of financial weakness and other prudential matters, and in other ways the Company currently cannot anticipate. FSOC-designated non-bank financial companies will also be required to prepare resolution plans, so-called living wills, that set out how they could most efficiently be liquidated if they endangered the U.S. financial system or the broader economy. The FSOC has made its initial SIFI designations, and the Company was not designated as such. However, the Company could be considered and designated at any time. Because the process is in its initial stages, the Company is at this time unable to predict the impact on an entity that is supervised as a SIFI by the Federal Reserve Board. The Company is not able to predict whether the capital requirements or other requirements imposed on SIFIs may impact the requirements applicable to the Company even if it is not designated as a SIFI. The uncertainty about regulatory requirements could influence the Company's product line or other business decisions with respect to some product lines. There is a similarly uncertain international designation process. The Financial Stability Board, appointed by the G-20 Summit, recently designated nine insurers as G-SIFIs, or global systemically-important insurers. As with the designation of SIFIs, it is unclear at this time how additional capital and other requirements affect the insurance and financial industries. The insurers designated as G-SIFIs to date represent organizations larger than the Company, but the possibility remains that the Company could be so designated.

Additionally, Dodd-Frank created the Consumer Financial Protection Bureau (CFPB), an independent division of the Department of Treasury with jurisdiction over credit, savings, payment, and other consumer financial products and services, other than investment products already regulated by the United States Securities and Exchange Commission (the SEC) or the U.S. Commodity Futures Trading Commission. CFPB has issued a rule to bring under its supervisory authority certain non-banks whose activities or products it determines pose risks to consumers. It is unclear at this time which activities or products will be covered by this rule. Certain of the Company's subsidiaries sell products that may be regulated by the CFPB. CFPB continues to bring enforcement actions involving a growing number of issues, including actions using state Attorney's General, which could directly or indirectly affect the Company or use any of its subsidiaries. Additionally, the CFPB is exploring the possibility of helping Americans manage their retirement savings and is considering the extent of its authority in that area. The Company is unable at this time to predict the impact of these activities on the Company.

Dodd-Frank includes a new framework of regulation of over-the-counter (OTC) derivatives markets which requires clearing of certain types of transactions which have been or are currently traded OTC by the Company. The types of transactions to be cleared are expected to increase in the future. The new framework could potentially impose additional costs, including increased margin requirements and additional regulation on

the Company. Increased margin

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requirements on the Company's part, combined with restrictions on securities that will qualify as eligible collateral, could continue to reduce its liquidity and require an increase in its holdings of cash and government securities with lower yields causing a reduction in income. The Company uses derivative financial instruments to mitigate a wide range of risks in connection with its businesses, including those arising from its variable annuity products with guaranteed benefit features. The derivative clearing requirements of Dodd-Frank could continue to increase the cost of the Company's risk mitigation and expose it to the risk of a default by a clearinghouse with respect to the Company's cleared derivative transactions.

Numerous provisions of Dodd-Frank require the adoption of implementing rules and/or regulations. The process of adopting such implementing rules and/or regulations have in some instances been delayed beyond the timeframes imposed by Dodd-Frank. Until the various final regulations are promulgated pursuant to Dodd-Frank, the full impact of the regulations on the Company will remain unclear. In addition, Dodd-Frank mandates multiple studies, which could result in additional legislation or regulation applicable to the insurance industry, the Company, its competitors or the entities with which the Company does business. Legislative or regulatory requirements imposed by or promulgated in connection with Dodd-Frank may impact the Company in many ways, including but not limited to the following: placing the Company at a competitive disadvantage relative to its competition or other financial services entities, changing the competitive landscape of the financial services sector and/or the insurance industry, making it more expensive for the Company to conduct its business, requiring the reallocation of significant company resources to government affairs, legal and compliance-related activities, causing historical market behavior or statistics utilized by the Company in connection with its efforts to manage risk and exposure to no longer be predictive of future risk and exposure or otherwise have a material adverse effect on the overall business climate as well as the Company's financial condition and results of operations.

The Company may be subject to regulation by the United States Department of Labor when providing a variety of products and services to employee benefit plans and individual investors that are governed by the Employee Retirement Income Security Act ( ERISA ). The Department of Labor is currently in the process of re-proposing a rule that would change the circumstances under which one who works with employee benefit plans and Individual Retirement Accounts would be considered a fiduciary under ERISA. Severe penalties are imposed for breach of duties under ERISA and the Company cannot predict the impact that the Department of Labor's re-proposed rule may have on its operations.

Certain life insurance policies, contracts, and annuities offered by the Company's subsidiaries are subject to regulation under the federal securities laws administered by the SEC. The federal securities laws contain regulatory restrictions and criminal, administrative, and private remedial provisions. From time to time, the SEC and the Financial Industry Regulatory Authority ( FINRA ) examine or investigate the activities of broker-dealers and investment advisors, including the Company's affiliated broker-dealers and investment advisors. These examinations or investigations often focus on the activities of the registered representatives and registered investment advisors doing business through such entities and the entities' supervision of those persons. It is possible that any examination or investigation could lead to enforcement action by the regulator and/or may result in payments of fines and penalties, payments to customers, or both, as well as changes in systems or procedures of such entities, any of which could have a material adverse effect on the Company's financial condition or results of operations.

In addition, the SEC is reviewing the standard of conduct applicable to brokers, dealers, and investment advisers when those entities provide personalized investment advice about securities to retail customers. FINRA has also issued a report addressing how its member firms might identify and address conflicts of interest including conflicts related to the introduction of new products and services and the compensation of the member firms' associated persons. These regulatory initiatives could have an impact on Company operations and the manner in which broker-dealers and investment advisers distribute the Company's products.

The Company may also be subject to regulation by governments of the countries in which it currently does, or may in the future, do, business, as well as regulation by the U.S. Government with respect to its operations in foreign countries, such as the Foreign Corrupt Practices Act. Penalties for violating the various laws governing the Company's business in other countries may include restrictions upon business operations, fines and imprisonment, both within the U.S. and abroad. U.S. enforcement of anti-corruption laws continues to increase in magnitude, and

penalties may be substantial.

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Other types of regulation that could affect the Company and its subsidiaries include insurance company investment laws and regulations, state statutory accounting and reserving practices, anti-trust laws, minimum solvency requirements, enterprise risk requirements, state securities laws, federal privacy laws, insurable interest laws, federal anti-money laundering and anti-terrorism laws, employment and immigration laws (including laws in Alabama where over half of the Company's employees are located), and because the Company owns and operates real property, state, federal, and local environmental laws. Under some circumstances, severe penalties may be imposed for breach of these laws.

The Company cannot predict what form any future changes to laws and/or regulations affecting participants in the financial services sector and/or insurance industry, including the Company and its competitors or those entities with which it does business, may take, or what effect, if any, such changes may have.

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

During the quarter ended June 30, 2014, the Company issued no securities in transactions which were not registered under the Securities Act of 1933, as amended (the Act).

*Purchases of Equity Securities by the Issuer*

During the six months ended June 30, 2014, the Company did not repurchase any of its common stock.



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**Item 6. Exhibits**

| <b>Item Number</b> | <b>Document</b>  |
|--------------------|--|
| 2*                 | Agreement and Plan of Merger, dated as of June 3, 2014, by and among the Dai-ichi Life Insurance Company, Limited, DL Investment (Delaware), Inc. and Protective Life Corporation, filed as Exhibit 2.1 to the Company's Current Report on Form 8-K filed June 4, 2014 (No. 001-11339).  |
| 3                  | Amended and Restated Bylaws of Protective Life Corporation adopted on February 25, 2013 (as restated to incorporate the June 3, 2014 amendment thereto), filed herewith.   |
| 10(a)              | Third Amended and Restated Reimbursement Agreement dated as of June 25, 2014, between Golden Gate III Vermont Captive Insurance Company and USB AG, Stamford Branch, filed herewith. ±   |
| 10(b)              | Employment Agreement, dated June 3, 2014, between the Company and John D. Johns, filed herewith.   |
| 10(c)              | Form of Employment Agreement between the Company and Executive Vice President, filed herewith  |
| 10(d)              | Form of Employment Agreement between the Company and Senior Vice President, filed herewith   |
| 31(a)              | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   |
| 31(b)              | Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   |
| 32(a)              | Certification Pursuant to 18 U.S.C Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 32(b)              | Certification Pursuant to 18 U.S.C Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.   |
| 101                | Financial statements from the quarterly report on Form 10-Q of Protective Life Corporation for the quarter ended June 30, 2014, filed on August 8, 2014, formatted in XBRL: (i) the Consolidated Condensed Statements of Income, (ii) the Consolidated Condensed Statements of Comprehensive Income (Loss), (iii) the Consolidated Condensed Balance Sheets, (iv) the Consolidated Condensed Statement of Shareowners' Equity, (v) the Consolidated Condensed Statements of Cash Flows, and (vi) the Notes to Consolidated Condensed Financial Statements. |

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\* Incorporated by Reference

± Certain portions of this Exhibit have been omitted pursuant to a request for confidential treatment. The non-public information has been filed separately with the Securities and Exchange Commission pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended.  
Management contract or compensatory plan or arrangement.

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**SIGNATURE**

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

PROTECTIVE LIFE CORPORATION

Date: August 8, 2014

By:

/s/ Steven G. Walker  
Steven G. Walker  
Senior Vice President, Controller  
and Chief Accounting Officer