

**PACIFIC MUTUAL HOLDING COMPANY
AND SUBSIDIARIES**

Consolidated Financial Statements
as of December 31, 2009 and 2008 and
for the years ended December 31, 2009, 2008 and 2007
and Independent Auditors' Report

INDEPENDENT AUDITORS' REPORT

Pacific Mutual Holding Company and Subsidiaries:

We have audited the accompanying consolidated statements of financial condition of Pacific Mutual Holding Company and Subsidiaries (the Company) as of December 31, 2009 and 2008, and the related consolidated statements of operations, equity and cash flows for each of the three years in the period ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Pacific Mutual Holding Company and Subsidiaries as of December 31, 2009 and 2008, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2009 in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1 to the consolidated financial statements, in 2009, the Company changed its method of accounting and reporting for other than temporary impairments of debt and equity securities.

As discussed in Note 1 to the consolidated financial statements, in 2009, the Company adopted new guidance requiring retrospective application and presentation requirements for noncontrolling interest (previously known as minority interest).

Deloitte & Touche LLP

March 4, 2010

Pacific Mutual Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
ASSETS		
Investments:		
Fixed maturity securities available for sale, at estimated fair value	\$26,682	\$22,604
Equity securities available for sale, at estimated fair value	375	219
Mortgage loans	6,577	5,622
Policy loans	6,509	6,920
Other investments	2,057	2,111
TOTAL INVESTMENTS	42,200	37,476
Cash and cash equivalents	2,060	3,888
Restricted cash	249	235
Deferred policy acquisition costs	4,857	5,028
Aircraft leasing portfolio, net	5,304	4,999
Other assets	2,720	3,852
Separate account assets	52,564	41,505
TOTAL ASSETS	\$109,954	\$96,983
LIABILITIES AND EQUITY		
Liabilities:		
Policyholder account balances	\$33,984	\$32,670
Future policy benefits	7,738	10,107
Short-term debt	539	799
Long-term debt	6,509	5,343
Other liabilities	2,241	2,227
Separate account liabilities	52,564	41,505
TOTAL LIABILITIES	103,575	92,651
Commitments and contingencies (Note 22)		
Members' Equity:		
Members' capital	6,537	5,928
Accumulated other comprehensive loss	(389)	(1,840)
Total Members' Equity	6,148	4,088
Noncontrolling interest	231	244
TOTAL EQUITY	6,379	4,332
TOTAL LIABILITIES AND EQUITY	\$109,954	\$96,983

See Notes to Consolidated Financial Statements

Pacific Mutual Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
REVENUES			
Policy fees and insurance premiums	\$2,446	\$2,103	\$1,792
Net investment income	1,897	2,029	2,157
Net realized investment gain (loss)	164	(767)	70
Other than temporary impairments consisting of \$642 in total, net of \$330 recognized in other comprehensive income (loss) for the year ended December 31, 2009	(312)	(584)	(98)
Realized investment gain on interest in PIMCO		109	
Investment advisory fees	208	255	327
Aircraft leasing revenue	578	571	535
Other income	230	294	266
TOTAL REVENUES	5,211	4,010	5,049
BENEFITS AND EXPENSES			
Interest credited to policyholder account balances	1,253	1,234	1,266
Policy benefits paid or provided	1,352	1,302	862
Commission expenses	705	723	690
Operating and other expenses	1,437	1,376	1,445
TOTAL BENEFITS AND EXPENSES	4,747	4,635	4,263
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE PROVISION (BENEFIT) FOR INCOME TAXES			
Provision (benefit) for income taxes	464	(625)	786
	24	(339)	112
INCOME (LOSS) FROM CONTINUING OPERATIONS			
Discontinued operations, net of taxes	(20)	(6)	11
Net income (loss)	420	(292)	685
Less: net (income) loss attributable to the noncontrolling interest from continuing operations	14	3	(38)
NET INCOME (LOSS) ATTRIBUTABLE TO THE COMPANY	\$434	(\$289)	\$647

See Notes to Consolidated Financial Statements

Pacific Mutual Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2009	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES	<i>(In Millions)</i>		
Net income (loss) excluding discontinued operations	\$440	(\$286)	\$674
Adjustments to reconcile net income (loss) excluding discontinued operations to net cash provided by operating activities:			
Net accretion on fixed maturity securities	(144)	(144)	(147)
Depreciation and amortization	281	259	256
Deferred income taxes	441	(535)	88
Net realized investment (gain) loss	(164)	767	(70)
Other than temporary impairments	312	584	98
Realized investment gain on interest in PIMCO		(109)	
Net change in deferred policy acquisition costs	(235)	(192)	(302)
Interest credited to policyholder account balances	1,253	1,234	1,266
Change in future policy benefits and other insurance liabilities	180	1,187	673
Other operating activities, net	154	(307)	(235)
NET CASH PROVIDED BY OPERATING ACTIVITIES BEFORE DISCONTINUED OPERATIONS	2,518	2,458	2,301
Net cash used in operating activities of discontinued operations	(27)	(18)	(71)
NET CASH PROVIDED BY OPERATING ACTIVITIES	2,491	2,440	2,230
CASH FLOWS FROM INVESTING ACTIVITIES			
Fixed maturity and equity securities available for sale:			
Purchases	(6,092)	(3,128)	(5,889)
Sales	1,916	2,167	2,142
Maturities and repayments	2,648	2,298	2,911
Repayments of mortgage loans	406	470	439
Fundings of mortgage loans and real estate	(1,434)	(1,665)	(1,660)
Change in policy loans	411	(510)	(342)
Sale of interest in PIMCO		288	
Change in restricted cash	(14)	(1)	60
Purchases of derivative instruments	(20)	(12)	(15)
Terminations of derivative instruments	7	301	(40)
Proceeds from nonhedging derivative settlements	168	781	19
Payments for nonhedging derivative settlements	(1,653)	(142)	(60)
Change in collateral received or pledged	(1,243)	1,029	17
Issuance of notes receivable on inventory financing	(603)	(1,214)	(1,153)
Repayments of notes receivable on inventory financing	673	1,382	988
Purchases of and advance payments on aircraft leasing portfolio	(561)	(694)	(646)
Acquisition of reinsurance business		(70)	
Other investing activities, net	41	(269)	66
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES BEFORE DISCONTINUED OPERATIONS	(5,350)	1,011	(3,163)
Net cash provided by investing activities of discontinued operations		7	76
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	(5,350)	1,018	(3,087)

(Continued)

See Notes to Consolidated Financial Statements

Pacific Mutual Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

<i>(Continued)</i>	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
CASH FLOWS FROM FINANCING ACTIVITIES			
Policyholder account balances:			
Deposits	\$8,003	\$7,320	\$6,876
Withdrawals	(7,972)	(7,602)	(7,131)
Net change in short-term debt	(260)	(52)	223
Issuance of long-term debt	1,642	335	1,013
Payments of long-term debt	(383)	(381)	(913)
Other financing activities, net	1	33	70
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	1,031	(347)	138
Net change in cash and cash equivalents	(1,828)	3,111	(719)
Cash and cash equivalents, beginning of year	3,888	777	1,496
CASH AND CASH EQUIVALENTS, END OF YEAR	\$2,060	\$3,888	\$777
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION			
Income taxes paid (received), net	(\$140)	(\$32)	\$48
Interest paid	\$201	\$271	\$349

See Notes to Consolidated Financial Statements

Pacific Mutual Holding Company and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

ORGANIZATION AND DESCRIPTION OF BUSINESS

Pacific Mutual Holding Company (PMHC) is a Nebraska mutual holding company organized pursuant to consent received from the California Department of Insurance and the implementation of a plan of conversion to form a mutual holding company structure in 1997 (the Conversion). The Conversion created PMHC and Pacific LifeCorp, an intermediate Delaware stock holding company. Pacific LifeCorp owns 100% of Pacific Life Insurance Company (Pacific Life), a Nebraska domiciled stock life insurance company.

Pacific Life transferred its legal domicile from the State of California to the State of Nebraska effective September 1, 2005. PMHC transferred its state of legal domicile from the State of California to the State of Nebraska, effective June 29, 2007, to reunite PMHC and Pacific Life under one regulatory authority.

PMHC and its subsidiaries and affiliates have primary business operations consisting of life insurance, individual annuities, mutual funds, pension and institutional products, and aircraft leasing. Effective December 31, 2009, Pacific LifeCorp contributed its 100% stock ownership of Aviation Capital Group Corp. (ACG) to Pacific Life. ACG is engaged in the acquisition and leasing of commercial jet aircraft.

BASIS OF PRESENTATION AND PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements of PMHC and its subsidiaries (the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and include the accounts of PMHC and its majority owned and controlled subsidiaries and variable interest entities (VIEs) in which the Company was determined to be the primary beneficiary. Noncontrolling interest is primarily comprised of private equity funds (Note 4). All significant intercompany transactions and balances have been eliminated in consolidation.

Pacific Life prepares its regulatory financial statements in accordance with statutory accounting practices prescribed or permitted by the Nebraska Department of Insurance (NE DOI), which is a comprehensive basis of accounting other than U.S. GAAP (Note 2).

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

In developing these estimates, management makes subjective and complex judgments that are inherently uncertain and subject to material change as facts and circumstances develop. Management has identified the following estimates as significant, as they involve a higher degree of judgment and are subject to a significant degree of variability:

- The fair value of investments in the absence of quoted market values
- Investment impairments
- Application of the consolidation rules to certain investments
- The fair value of and accounting for derivatives
- Aircraft valuation and impairment
- The capitalization and amortization of deferred policy acquisition costs (DAC)
- The liability for future policyholder benefits
- Accounting for income taxes and the valuation of deferred income tax assets and liabilities and unrecognized tax benefits
- Accounting for reinsurance transactions
- Litigation and other contingencies

Certain reclassifications have been made to the 2008 and 2007 consolidated financial statements to conform to the 2009 financial statement presentation.

RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

Effective September 30, 2009, the Company adopted the Financial Accounting Standards Board (FASB) Accounting Standards Codification (Codification) as the single source of authoritative U.S. GAAP. The Codification does not create new accounting and reporting guidance, rather it reorganized then-existing U.S. GAAP pronouncements into approximately 90 Topics within a consistent structure. All guidance in the Codification carries an equal level of authority. After the effective date of the Codification, all nongrandfathered accounting literature not included in the Codification is superseded and deemed nonauthoritative. Adoption of the Codification also changed how the Company references U.S. GAAP in its consolidated financial statements.

In April 2009, the FASB issued additional guidance under the Codification's Fair Value Measurements and Disclosures Topic. This update relates to determining fair values when there is no active market or where the price inputs being used represent distressed sales. The Company early adopted this guidance on March 31, 2009. This update provides additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased. Also included is guidance on identifying circumstances that indicate a transaction is not orderly. The adoption of this guidance resulted in an increase of \$436 million to the estimated fair value and a resulting decrease of \$436 million to gross unrealized investment loss of residential mortgage-backed securities (RMBS) as of March 31, 2009. As of December 31, 2009, the year to date effect of this adoption was an increase of \$214 million to the estimated fair value and a decrease of \$214 million to the gross unrealized investment loss of RMBS. See Note 15 for information on the Company's fair value measurements and expanded disclosures.

In April 2009, the FASB issued additional guidance under the Codification's Investments – Debt and Equity Securities Topic. For debt securities, this guidance replaces the management assertion that it has the intent and ability to hold an impaired debt security until recovery with the requirement that management assert if it either has the intent to sell the debt security or if it is more likely than not the entity will be required to sell the debt security before recovery of its amortized cost basis. If management intends to sell the debt security or it is more likely than not the entity will be required to sell the debt security before recovery of its amortized cost basis, an other than temporary impairment (OTTI) shall be recognized in earnings equal to the entire difference between the debt security's amortized cost basis and its fair value at the reporting date. After the recognition of an OTTI, the debt security is accounted for as if it had been purchased on the measurement date of the OTTI, with an amortized cost basis equal to the previous amortized cost basis less the OTTI recognized in earnings. The update also changes the presentation in the financial statements of non credit related impairment amounts for instruments within its scope. When the entity asserts it does not have the intent to sell the security and it is more likely than not it will not have to sell the security before recovery of its amortized cost basis, only the credit related impairment losses are to be recognized in earnings and non credit losses are to be recognized in other comprehensive income (OCI). Additionally, this update provides for enhanced presentation and disclosure of OTTIs of debt and equity securities in the consolidated financial statements. The Company early adopted this guidance effective January 1, 2009, resulting in an after tax decrease to OCI of \$170 million, including an after tax DAC impact of \$5 million, and an after tax increase to retained earnings of \$175 million.

Effective January 1, 2009, the FASB issued additional guidance to the Codification's Consolidation Topic. This guidance improves the relevance, comparability and transparency of the financial information that a company provides in its consolidated financial statements by establishing accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. As a result of the adoption of this guidance, which required retrospective application of presentation requirements, total equity as of December 31, 2008 and 2007, increased by \$244 million and \$214 million, respectively, representing the noncontrolling interest, and other liabilities and total liabilities as of December 31, 2008 and 2007 decreased by \$244 million and \$214 million, respectively, as a result of reclassifying noncontrolling interest (previously known as minority interest) to equity.

Effective January 1, 2007, the FASB issued additional guidance to the Codification's Financial Services – Insurance Topic. This guidance governs the accounting for DAC on internal replacements on insurance and investment contracts. This guidance defines an internal replacement as a modification in product benefits, features, rights, or coverages that occur by the exchange of a contract for a new contract, or by amendment, endorsement, or rider to a contract, or by the election of a feature or coverage within a contract. The adoption of this guidance resulted in a reduction to DAC and the Company recorded a cumulative effect adjustment of \$29 million, after tax, which was recorded as a reduction to retained earnings during the year ended December 31, 2007.

INVESTMENTS

Fixed maturity and equity securities available for sale are reported at estimated fair value, with unrealized gains and losses, net of adjustments related to DAC, future policy benefits and deferred income taxes, recorded as a component of OCI. For mortgage-backed securities and asset-backed securities included in fixed maturity securities available for sale, the Company recognizes income using a constant effective yield based on anticipated prepayments and the estimated economic life of the securities. When estimates of prepayments change, the effective yield is recalculated to reflect actual payments to date and anticipated future

payments. For fixed rate securities, the net investment in the securities is adjusted to the amount that would have existed had the new effective yield been applied since the acquisition of the securities. These adjustments are reflected in net investment income. Trading securities are reported at estimated fair value with changes in estimated fair value included in net realized investment gain (loss).

Investment income consists primarily of interest and dividends, net investment income from partnership interests, prepayment fees on fixed maturity securities and mortgage loans, and income from certain derivatives. Interest is recognized on an accrual basis and dividends are recorded on the ex-dividend date. Amortization of premium and accretion of discount on fixed maturity securities is recorded using the effective interest method.

The Company's available for sale securities are regularly assessed for OTTI. If a decline in the estimated fair value of an available for sale security is deemed to be other than temporary, the OTTI is recorded equal to the difference between the estimated fair value and net carrying amount of the security. If the OTTI for a debt security is attributable to both credit and other factors, then the OTTI is bifurcated and the non credit related portion is recorded to OCI while the credit portion is recorded as a net realized investment loss. If the OTTI is related to credit factors only, it is recorded as a net realized investment loss.

The evaluation of OTTIs is a quantitative and qualitative process subject to significant estimates and management judgment. The Company has rigorous controls and procedures in place to monitor securities and identify those that are subject to greater analysis for OTTIs. The Company has an investment impairment committee comprised of investment and accounting professionals that reviews and evaluates securities for potential OTTIs at least on a quarterly basis.

In evaluating whether a decline in value is other than temporary, the Company considers many factors including, but not limited to, the following: the extent and duration of the decline in value; the reasons for the decline (credit event, currency, or interest-rate related, including spread widening); the ability and intent to hold the investment for a period of time to allow for a recovery of value; and the financial condition of and near-term prospects of the issuer.

Analysis of the probability that all cash flows will be collected under the contractual terms of a fixed maturity security and determination as to whether the Company does not intend to sell the security and that it is more likely than not that the Company will not be required to sell the security before recovery of the investment were key factors in determining whether a fixed maturity security is other than temporarily impaired.

For mortgage-backed and asset-backed securities, scrutiny was placed on the performance of the underlying collateral and projected future cash flows. In projecting future cash flows, the Company incorporates inputs from third-party sources and applies reasonable judgment in developing assumptions used to estimate the probability and timing of collecting all contractual cash flows.

In evaluating investment grade perpetual preferred securities, which do not have final contractual cash flows, the Company applied OTTI considerations used for debt securities, placing emphasis on the probability that all cash flows will be collected under the contractual terms of the security and the Company's intent and ability to hold the security to allow for a recovery of value. Perpetual preferred securities are reported as equity securities as they are structured in equity form, but have significant debt-like characteristics, including periodic dividends, call features, and credit ratings and pricing similar to debt securities. The *SEC Issues Letter Clarifying Other-Than-Temporary Impairment Guidance for Perpetual Preferred Securities* issued on October 15, 2008 states that if an investor holds a perpetual preferred security with an estimated fair value below cost that is not attributable to the credit deterioration of the issuer, then the investor would not be required to recognize an OTTI by asserting that it has the intent and ability to continue holding the security for a sufficient period to allow for an anticipated recovery in market value.

Realized gains and losses on investment transactions are determined on a specific identification basis and are included in net realized investment gain (loss).

Mortgage loans on real estate are carried at their unpaid principal balance, net of deferred origination fees and write-downs. Mortgage loans are considered to be impaired when management estimates that based upon current information and events, it is probable that the Company will not be able to collect amounts due according to the contractual terms of the mortgage loan agreement. For mortgage loans deemed to be impaired, a write-down is taken for the difference between the carrying amount and the Company's estimate of the present value of the expected future cash flows discounted at the current market rate and recorded in net realized investment gain (loss). As of December 31, 2009, two loans totaling \$8 million were considered impaired, however no valuation allowance was necessary as the fair value of the collateral was greater than the carrying amount of the related loans. The Company had no write-downs during the years ended December 31, 2009, 2008 and 2007. Policy loans are stated at unpaid principal balances.

Other investments primarily consist of partnership and joint ventures, real estate investments, derivative instruments, non-marketable equity securities, and low income housing related investments qualifying for tax credits (LIHTC). Partnership and joint

venture interests where the Company does not have a controlling interest or majority ownership are recorded under the cost or equity method of accounting depending on the equity ownership position. Real estate investments are carried at depreciated cost, net of write-downs, or, for real estate acquired in satisfaction of debt, estimated fair value less estimated selling costs at the date of acquisition, if lower than the related unpaid balance.

Investments in LIHTC are recorded under either the effective interest method, if they meet certain requirements, including a projected positive yield based solely on guaranteed credits, or are recorded under the equity method if these certain requirements are not met. For investments in LIHTC recorded under the effective interest method, the amortization of the original investment and the tax credits are recorded in the provision (benefit) for income taxes. For investments in LIHTC recorded under the equity method, the amortization of the initial investment is included in net investment income, and the related tax credits are recorded in the provision (benefit) for income taxes (Note 19). The amortization recorded in net investment income was \$3 million, \$5 million and \$20 million for the years ended December 31, 2009, 2008 and 2007, respectively.

All derivatives, whether designated in hedging relationships or not, are required to be recorded at estimated fair value. If the derivative is designated as a cash flow hedge, the effective portion of changes in the estimated fair value of the derivative is recorded in OCI and recognized in earnings when the hedged item affects earnings. If the derivative is designated as a fair value hedge, the changes in the estimated fair value of the derivative and the hedged item are recognized in net realized investment gain (loss). The change in value of the hedged item associated with the risk being hedged is reflected as an adjustment to the carrying amount of the hedged item. For derivative instruments not designated as hedges, the change in estimated fair value of the derivative is recorded in net realized investment gain (loss). Estimated fair value exposure is calculated based on the aggregate estimated fair value of all derivative instruments with each counterparty, net of collateral received, in accordance with legally enforceable counterparty master netting agreements (Note 11).

The periodic cash flows for all hedging derivatives are recorded consistent with the hedged item on an accrual basis. For derivatives that are hedging securities, these amounts are included in net investment income. For derivatives that are hedging liabilities, these amounts are included in interest credited to policyholder account balances. For derivatives not designated as hedging instruments, the periodic cash flows are reflected in net realized investment gain (loss) on an accrual basis. Upon termination of a cash flow hedging relationship, the accumulated amount in OCI is amortized into net investment income or interest credited to policyholder account balances over the remaining life of the hedged item. Upon termination of a fair value hedging relationship, the accumulated adjustment to the carrying value of the hedged item is amortized into net investment income, interest expense or interest credited to policyholder account balances over its remaining life.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include all investments with an original maturity of three months or less. The Company entered into a series of Federal National Mortgage Association (FNMA) pass-through dollar roll transactions during the fourth quarter of 2008. The Company purchased FNMA pass through securities and was contractually obligated to resell the same or substantially the same securities within 30 days of purchase. The Company classified these dollar roll transactions as short-term secured loans and reported them as cash and cash equivalents. As of December 31, 2009 and 2008, the loans amounted to zero and \$403 million, respectively. The fair values of the securities held in connection with the secured lending were zero and \$410 million as of December 31, 2009 and 2008, respectively.

RESTRICTED CASH

Restricted cash primarily consists of security deposits, commitment fees, maintenance reserve payments, supplemental rental payments and rental payments received from certain lessees related to the aircraft leasing business.

DEFERRED POLICY ACQUISITION COSTS

The costs of acquiring new insurance business, principally commissions, medical examinations, underwriting, policy issue and other expenses, all of which vary with and are primarily associated with the production of new business, are deferred and recorded as an asset commonly referred to as DAC. DAC related to internally replaced contracts (as defined in the Codification's Financial Services – Insurance Topic), is immediately written off to expense and any new deferrable expenses associated with the replacement are deferred if the contract modification substantially changes the contract. However, if the contract modification does not substantially change the contract, the existing DAC asset remains in place and any acquisition costs associated with the modification are immediately expensed. As of December 31, 2009 and 2008, the carrying value of DAC was \$4.9 billion and \$5.0 billion, respectively (Note 8).

For universal life (UL), variable annuities and other investment-type contracts, acquisition costs are amortized through earnings in proportion to the present value of estimated gross profits (EGPs) from projected investment, mortality and expense margins, and

surrender charges over the estimated lives of the contracts. Actual gross margins or profits may vary from management's estimates, which can increase or decrease the rate of DAC amortization. DAC related to traditional policies is amortized through earnings over the premium-paying period of the related policies in proportion to premium revenues recognized, using assumptions and estimates consistent with those used in computing policy reserves. DAC related to certain unrealized components in OCI, primarily unrealized gains and losses on securities available for sale, is recorded directly to equity through OCI.

Significant assumptions in the development of EGPs include investment returns, surrender and lapse rates, rider utilization, interest spreads, and mortality margins. The Company's long-term assumption for the underlying separate account investment return ranges up to 8.0%.

A change in the assumptions utilized to develop EGPs results in a change to amounts expensed in the reporting period in which the change was made by adjusting the DAC balance to the level DAC would have been had the EGPs been calculated using the new assumptions over the entire amortization period. In general, favorable experience variances result in increased expected future profitability and may lower the rate of DAC amortization, whereas unfavorable experience variances result in decreased expected future profitability and may increase the rate of DAC amortization. All critical assumptions utilized to develop EGPs are evaluated at least annually and necessary revisions are made to certain assumptions to the extent that actual or anticipated experience necessitates such a prospective change (Note 8).

The Company defers sales inducements and amortizes them over the life of the policy using the same methodology and assumptions used to amortize DAC. The Company offers a sales inducement to the policyholder where the policyholder receives a bonus credit, typically ranging from 0.5% to 8.0% of each deposit. The capitalized sales inducement balance included in the DAC asset was \$583 million and \$552 million as of December 31, 2009 and 2008, respectively.

AIRCRAFT LEASING PORTFOLIO

Aircraft are recorded at cost, which includes certain acquisition costs, less accumulated depreciation. Major improvements to aircraft are capitalized when incurred. The Company evaluates carrying values of aircraft based upon changes in market and other physical and economic conditions and will record impairment losses to recognize a loss in the value of the aircraft when management believes that, based on estimated future cash flows, the recoverability of the Company's investment in an aircraft is unlikely (Note 10). The Company had four and two non-earning aircraft in the portfolio as of December 31, 2009 and 2008, respectively.

GOODWILL FROM ACQUISITIONS

Goodwill represents the excess of costs over the fair value of net assets acquired. Goodwill is not amortized but is reviewed for impairment at least annually or more frequently if events occur or circumstances indicate that the goodwill might be impaired. Goodwill from acquisitions, included in other assets, totaled \$43 million as of December 31, 2009 and 2008. There were no goodwill impairment write-downs from continuing operations during the years ended December 31, 2009, 2008 and 2007.

TRADE AND FINANCE RECEIVABLES

Pacific Asset Funding, LLC (PAF), a Delaware limited liability company, is a wholly owned subsidiary of Pacific LifeCorp. PAF and its subsidiaries offer a broad range of trade finance and inventory procurement services to corporations and logistics and trading companies.

Inventory, which is included in other assets, is stated at the lower of cost or market. PAF uses the specific identification method to value all inventories. Inventories consist of finished products held for sale. As of December 31, 2009 and 2008, inventory was \$12 million and \$16 million, respectively. Inventory sales revenue and cost of goods sold are recorded when the title of goods passes to the buyer and the buyer assumes the risks and rewards of ownership and are included in other income and operating and other expenses, respectively.

POLICYHOLDER ACCOUNT BALANCES

Policyholder account balances on UL and investment-type contracts, such as funding agreements, annuity and deposit liabilities and guaranteed interest contracts (GICs), are valued using the retrospective deposit method and are equal to accumulated account values, which consist of deposits received, plus interest credited, less withdrawals and assessments (Note 12). Interest credited to these contracts primarily ranged from 0.2% to 9.0%.

FUTURE POLICY BENEFITS

Annuity reserves, which primarily consist of group retirement and structured settlement annuities, are equal to the present value of estimated future payments using pricing assumptions, as applicable, for interest rates, mortality, morbidity, retirement age and expenses (Note 12). Interest rates used in establishing such liabilities ranged from 1.6% to 11.3%.

The Company offers a rider on certain variable annuity contracts that guarantees net principal over a ten-year holding period, as well as riders on certain variable annuity contracts that guarantee a minimum withdrawal benefit over specified periods, subject to certain restrictions. These variable annuity guaranteed living benefits (GLBs) are considered embedded derivatives and are recorded in future policy benefits (Note 12).

Policy charges assessed against policyholders that represent compensation to the Company for services to be provided in future periods, or unearned revenue reserves (URR), are recognized in revenue over the expected life of the contract using the same methods and assumptions used to amortize DAC. Unearned revenue related to certain unrealized components in OCI, primarily unrealized gains and losses on securities available for sale, is recorded directly to equity through OCI.

Life insurance reserves are valued using the net level premium method on the basis of actuarial assumptions appropriate at policy issue. Mortality and persistency assumptions are generally based on the Company's experience, which, together with interest and expense assumptions, include a margin for possible unfavorable deviations. Interest rate assumptions ranged from 3.0% to 9.3%. Future dividends for participating business are provided for in the liability for future policy benefits.

As of December 31, 2009 and 2008, participating experience rated policies paying dividends represent less than 1% of direct life insurance in force.

Estimates of future policy benefit reserves and liabilities are continually reviewed and, as experience develops, are adjusted as necessary. Such changes in estimates are included in earnings for the period in which such changes occur.

REINSURANCE

The Company has ceded reinsurance agreements with other insurance companies to limit potential losses, reduce exposure arising from larger risks, provide additional capacity for future growth, and assumed reinsurance agreements intended to offset reinsurance costs. As part of a strategic alliance, the Company also reinsures risks associated with policies written by an independent producer group through modified coinsurance and yearly renewable term arrangements with this producer group's reinsurance company.

All assets associated with business reinsured on a modified coinsurance basis remain with, and under the control of, the Company. As part of its risk management process, the Company routinely evaluates its reinsurance programs and may change retention limits, reinsurers or other features at any time.

Reinsurance accounting is utilized for ceded transactions when risk transfer provisions have been met. To meet risk transfer requirements, a reinsurance contract must include insurance risk, consisting of both underwriting and timing risk, and a reasonable possibility of a significant loss to the reinsurer.

Reinsurance premiums ceded and reinsurance recoveries on benefits and claims incurred are deducted from their respective revenue and benefit and expense accounts. Prepaid reinsurance premiums, included in other assets, are premiums that are paid in advance for future coverage. Reinsurance recoverables, included in other assets, include balances due from reinsurance companies for paid and unpaid losses. Amounts receivable and payable are offset for account settlement purposes for contracts where the right of offset exists. See Note 17.

REVENUES, BENEFITS AND EXPENSES

Insurance premiums, annuity contracts with life contingencies and traditional life and term insurance contracts, are recognized as revenue when due. Benefits and expenses are matched against such revenues to recognize profits over the lives of the contracts. This matching is accomplished by providing for liabilities for future policy benefits, expenses of contract administration and the amortization of DAC and URR.

Receipts for UL and investment-type contracts are reported as deposits to either policyholder account balances or separate account liabilities, and are not included in revenue. Policy fees consist of mortality charges, surrender charges and expense charges that have been earned and assessed against related account values during the period. The timing of policy fee revenue recognition is determined based on the nature of the fees. Benefits and expenses include policy benefits and claims incurred in the

period that are in excess of related policyholder account balances, interest credited to policyholder account balances, expenses of contract administration and the amortization of DAC.

Investment advisory fees are primarily fees earned from Pacific Life Fund Advisors LLC (PLFA), a wholly owned subsidiary of Pacific Life formed in 2007, which serves as the investment advisor for the Pacific Select Fund, an investment vehicle provided to the Company's variable universal life (VUL) and variable annuity contract holders, and the Pacific Life Funds, the investment vehicle for the Company's mutual fund products. These fees are based upon the net asset value of the underlying portfolios, and are recorded as earned. Related subadvisory expense is included in operating and other expenses and recorded when incurred.

Aircraft leases, which are structured as triple net leases, are accounted for as operating leases. Aircraft leasing revenue is recognized ratably over the terms of the lease agreements. ACG has four capital leases, which are accounted for under the provisions in the Codification's Leases Topic. As of December 31, 2009 and 2008, capital leases in the amount of \$8 million and \$11 million, respectively, are classified in other assets.

DEPRECIATION AND AMORTIZATION

Aircraft and certain other assets are depreciated or amortized using the straight-line method over estimated useful lives, which range from three to 40 years. Depreciation and amortization of aircraft under operating leases and certain other assets are included in operating and other expenses. Depreciation of investment real estate is computed using the straight-line method over estimated useful lives, which range from five to 30 years. Depreciation of investment real estate is included in net investment income.

INCOME TAXES

PMHC files a consolidated Federal income tax return and a combined California franchise tax return with its includable subsidiaries. Certain of the Company's non-insurance subsidiaries also file separate state tax returns, if necessary. Pacific Alliance Reinsurance Ltd. (PAR Bermuda), a Bermuda-based life reinsurance company wholly owned by Pacific LifeCorp, files a separate Federal tax return. Pacific Life and its wholly owned, Arizona domiciled life insurance subsidiary, Pacific Life & Annuity Company (PL&A), Pacific Alliance Reinsurance Company of Vermont (PAR Vermont), a Vermont-based life reinsurance company wholly owned by Pacific Life, and PAR Bermuda are taxed as life insurance companies for Federal income tax purposes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years the differences are expected to be recovered or settled.

CONTINGENCIES

Each reporting cycle the Company evaluates all identified contingent matters on an individual basis. A loss is recorded if probable and reasonably estimable. The Company establishes reserves for these contingencies at the best estimate, or, if no one number within the range of possible losses is more probable than any other, the Company records an estimated reserve at the low end of the range of losses. See Note 22.

SEPARATE ACCOUNTS

Separate accounts primarily include variable annuity and life contracts, as well as other guaranteed and non-guaranteed accounts. Separate account assets are recorded at estimated fair value and represent legally segregated contract holder funds. A separate account liability is recorded equal to the amount of separate account assets. Deposits to separate accounts, investment income and realized and unrealized gains and losses on the separate account assets accrue directly to contract holders and, accordingly, are not reflected in the consolidated statements of operations or cash flows. Amounts charged to the separate account for mortality, surrender and expense charges are included in revenues as policy fees.

For separate account funding agreements in which the Company provides a guarantee of principal and interest to the contract holder and bears all the risks and rewards of the investments underlying the separate account, the related investments and liabilities are recognized as investments and liabilities in the consolidated statements of financial condition. Revenue and expenses are recognized within the respective revenue, and benefit and expense lines in the consolidated statements of operations.

FAIR VALUE OF FINANCIAL INSTRUMENTS

The estimated fair value of financial instruments, disclosed in Notes 9, 11 and 15, has been determined using available market information and appropriate valuation methodologies. However, considerable judgment is often required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented may not be indicative of the amounts the Company could

realize in a current market exchange. The use of different market assumptions and/or estimation methodologies could have a significant effect on the estimated fair value amounts.

2. STATUTORY FINANCIAL INFORMATION AND DIVIDEND RESTRICTIONS

STATUTORY ACCOUNTING PRACTICES

The Company's principal life insurance subsidiary, Pacific Life, prepares its regulatory statutory financial statements in accordance with statutory accounting practices prescribed or permitted by the NE DOI, which is a comprehensive basis of accounting other than U.S. GAAP. Statutory accounting practices primarily differ from U.S. GAAP by charging policy acquisition costs to expense as incurred, recognizing certain policy fees as revenue when billed, establishing future policy benefit liabilities using different actuarial assumptions, reporting surplus notes as surplus instead of debt, as well as valuing investments and certain assets and accounting for deferred income taxes on a different basis.

As of December 31, 2009, Pacific Life had one permitted practice approved by the NE DOI that differed from statutory accounting practices adopted by the National Association of Insurance Commissioners (NAIC). This permitted practice relates to the valuation of certain statutory separate account assets that are carried at book value instead of estimated fair value. Pacific Life's statutory capital and surplus as of December 31, 2009 and 2008 did not reflect unrealized losses of \$29 million and \$88 million, respectively, with regards to this permitted practice. Pacific Life had a second permitted practice with a financial statement filing date of December 31, 2008 that expired on December 30, 2009. This permitted practice allowed Pacific Life to apply the revised version of Actuarial Guideline 39 (AG 39) for variable annuity reserves that is contained in the final recommendations submitted by the Capital & Surplus Relief Working Group to the Executive Committee of the NAIC. This permitted practice resulted in lowering statutory reserves by \$442 million as of December 31, 2008.

In addition, Pacific Life uses a NE DOI prescribed accounting practice for certain synthetic GIC reserves that differs from statutory accounting practices adopted by the NAIC. As of December 31, 2009 and 2008, this NE DOI prescribed accounting practice resulted in statutory reserves of \$20 million and \$12 million, respectively, as opposed to statutory reserves of zero and \$640 million, respectively, using statutory accounting practices adopted by the NAIC.

STATUTORY NET INCOME (LOSS) AND SURPLUS

Statutory net income (loss) of Pacific Life was \$652 million, (\$1,529) million and \$362 million for the years ended December 31, 2009, 2008 and 2007, respectively. Statutory capital and surplus of Pacific Life was \$5,006 million and \$3,136 million as of December 31, 2009 and 2008, respectively.

RISK-BASED CAPITAL

Risk-based capital is a method developed by the NAIC to measure the minimum amount of capital appropriate for an insurance company to support its overall business operations in consideration of its size and risk profile. The formulas for determining the amount of risk-based capital specify various weighting factors that are applied to financial balances or various levels of activity based on the perceived degree of risk. Additionally, certain risks are required to be measured using actuarial cash flow modeling techniques, subject to formulaic minimums. The adequacy of a company's actual capital is measured by a comparison to the risk-based capital results. Companies below minimum risk-based capital requirements are classified within certain levels, each of which requires specified corrective action. As of December 31, 2009 and 2008, Pacific Life, PL&A and PAR Vermont exceeded the minimum risk-based capital requirements.

DIVIDEND RESTRICTIONS

The payment of dividends by Pacific Life to Pacific LifeCorp is subject to restrictions set forth in the State of Nebraska insurance laws. These laws require (i) notification to the NE DOI for the declaration and payment of any dividend and (ii) approval by the NE DOI for accumulated dividends within the preceding twelve months that exceed the greater of 10% of statutory policyholder surplus as of the preceding December 31 or statutory net gain from operations for the preceding twelve months ended December 31. Generally, these restrictions pose no short-term liquidity concerns for Pacific LifeCorp. Based on these restrictions and 2009 statutory results, Pacific Life could pay \$629 million in dividends in 2010 to Pacific LifeCorp without prior approval from the NE DOI, subject to the notification requirement.

No dividends were paid during 2009 and 2007. During the year ended December 31, 2008, Pacific Life paid a cash dividend to Pacific LifeCorp of \$345 million.

The maximum amount of ordinary dividends that can be paid by PL&A to Pacific Life without restriction cannot exceed the lesser of 10% of statutory surplus as regards to policyholders, or the statutory net gain from operations. Based on this limitation and 2009 statutory results, PL&A could pay \$23 million in dividends to Pacific Life in 2010 without prior regulatory approval. No dividends were paid during 2009, 2008 and 2007.

OTHER

The Company has reinsurance contracts in place with a reinsurer whose financial stability has been deteriorating. In January 2009, the reinsurer's domiciliary state regulator issued an order of supervision, which requires the regulator's consent to any transaction outside the normal course of business. The Company will continue to monitor the events surrounding this reinsurer and evaluate its options to deal with any further deterioration of this reinsurer's financial condition. As of December 31, 2009, statutory reserves ceded to this reinsurer amounted to approximately \$162 million.

3. CLOSED BLOCK

In connection with the Conversion, an arrangement known as a closed block (the Closed Block) was established, for dividend purposes only, for the exclusive benefit of certain individual life insurance policies that had an experience based dividend scale for 1997. The Closed Block was designed to give reasonable assurance to holders of the Closed Block policies that policy dividends will not change solely as a result of the Conversion.

Assets that support the Closed Block, which are primarily included in fixed maturity securities and policy loans, amounted to \$285 million and \$278 million as of December 31, 2009 and 2008, respectively. Liabilities allocated to the Closed Block, which are primarily included in future policy benefits, amounted to \$307 million and \$311 million as of December 31, 2009 and 2008, respectively. The net contribution to income from the Closed Block was \$4 million, \$1 million and \$1 million for the years ended December 31, 2009, 2008 and 2007, respectively.

4. VARIABLE INTEREST ENTITIES

The following table presents, as of December 31, 2009 and 2008, the total assets and maximum exposure to loss relating to VIEs, which the Company (i) has consolidated because it is the primary beneficiary or (ii) holds a significant variable interest, but has not consolidated because it is not the primary beneficiary:

	Primary Beneficiary		Not Primary Beneficiary	
	Total Assets	Maximum Exposure to Loss	Total Assets	Maximum Exposure to Loss
<i>(In Millions)</i>				
<u>December 31, 2009:</u>				
Aircraft securitizations	\$2,642	\$218 ⁽¹⁾	\$371	
Private equity funds	239	30		
Asset-backed securities			1,910	\$103
Total	\$2,881	\$248	\$2,281	\$103
<u>December 31, 2008:</u>				
Aircraft securitizations	\$2,777	\$145 ⁽¹⁾	\$427	
Private equity funds	236	30		
Asset-backed securities			3,816	\$93
Total	\$3,013	\$175	\$4,243	\$93

⁽¹⁾ Excludes contingent purchase obligations (Note 22) totaling \$100 million and \$50 million as of December 31, 2009 and 2008, respectively.

AIRCRAFT SECURITIZATIONS

ACG has sponsored three financial asset securitizations secured by interests in aircraft. ACG serves as the remarketing agent and provides various aircraft related services in all three securitizations for a fee. This fee is eliminated for the two consolidated securitizations and is included in other income as earned for the unconsolidated securitization.

In 2005, ACG sponsored a securitization transaction whereby ACG Trust III acquired 74 of ACG's aircraft through a private placement note offering in the amount of \$1,860 million. ACG receives all of the expected residual return from ACG Trust III. Therefore, ACG was determined to be the primary beneficiary of this VIE and ACG Trust III is consolidated into the consolidated financial statements of the Company. These private placement notes are the obligation of ACG Trust III and represent debt that is non-recourse to the Company (Note 14). Non-recourse debt consolidated from ACG Trust III was \$1,309 million and \$1,445 million as of December 31, 2009 and 2008, respectively. As of December 31, 2009 and 2008, the maximum exposure to loss, based on carrying value, was \$130 million and \$72 million, respectively. Consolidated assets are reported in aircraft leasing portfolio, net, restricted cash and other assets. Consolidated liabilities are reported in long-term debt and other liabilities.

In 2003, ACG sponsored a securitization transaction whereby Aviation Capital Group Trust II (ACG Trust II) acquired 37 of ACG's aircraft through a private placement note offering in the amount of \$1,027 million. ACG owns 100% of the equity of ACG Trust II and absorbs any losses in the trust up to ACG's equity interest. Therefore, ACG was determined to be the primary beneficiary of this VIE and ACG Trust II is consolidated into the consolidated financial statements of the Company. These private placement notes are the obligation of ACG Trust II and represent debt that is non-recourse to the Company (Note 14). Non-recourse debt consolidated from ACG Trust II was \$666 million and \$728 million as of December 31, 2009 and 2008, respectively. As of December 31, 2009 and 2008, the maximum exposure to loss, based on carrying value, was \$88 million and \$73 million, respectively. Consolidated assets are reported in aircraft leasing portfolio, net, restricted cash and other assets. Consolidated liabilities are reported in long-term debt and other liabilities.

In 2000, ACG sponsored a financial asset securitization of aircraft to Aviation Capital Group Trust (Aviation Trust). ACG and Pacific Life are beneficial interest holders in Aviation Trust. Aviation Trust is not consolidated as the Company is not the primary beneficiary. The carrying value is comprised of beneficial interests issued by Aviation Trust. As of December 31, 2009 and 2008, the maximum exposure to loss, based on carrying value, was zero.

PRIVATE EQUITY FUNDS

Private equity funds (the Funds) are three limited partnerships that invest in private equity investments for outside investors, where the Company is the general partner. The Company provides investment management services to the Funds for a fee and receives carried interest based upon the performance of the Funds and is a VIE due to the lack of control by the other equity investors. The Company has not guaranteed the performance, liquidity or obligations of the Funds, and the Company's maximum exposure to loss is equal to the carrying amounts of its retained interest. VIE debt consolidated from the Funds was \$2 million as of December 31, 2009 and 2008. Consolidated assets are reported in other investments and cash and cash equivalents and consolidated liabilities are reported in long-term debt.

ASSET-BACKED SECURITIES

As part of the Company's investment strategy, the Company purchases primarily investment grade beneficial interests issued from bankruptcy-remote special purpose entities (SPEs), which are collateralized by financial assets including corporate debt. The Company has not guaranteed the performance, liquidity or obligations of the SPEs, and the Company's maximum exposure to loss is limited to its carrying value of the beneficial interests in the SPEs. The Company has no liabilities related to these VIEs. The Company has determined that it is not the primary beneficiary of these entities as the Company does not absorb a majority of the expected losses or receive a majority of the expected residual return. The Company does not consolidate these entities. The investments are reported as fixed maturity securities available for sale and had a net carrying amount of \$103 million and \$93 million at December 31, 2009 and 2008, respectively. During the years ended December 31, 2009 and 2008, the Company recorded OTTI's of \$60 million and \$117 million, respectively, related to these securities.

FUTURE ACCOUNTING CHANGE

Effective January 1, 2010, the Company will change the methodology it employs to determine if an entity is a VIE and, once identified, if a VIE should be included in the consolidated financial statements. The new methodology will place more emphasis on the Company's ability to direct the activities that most significantly impact the entity's financial performance. The Company will examine anew all entities previously identified as VIEs. The Company does not expect this change to have a material impact on its consolidated financial statements.

5. INTEREST IN PIMCO

As of December 31, 2007, the Company owned a beneficial economic interest in Pacific Investment Management Company LLC (PIMCO) through Allianz Global Investors of America LLC (interest in PIMCO). PIMCO offers investment products through managed accounts and institutional, retail and offshore mutual funds. The interest in PIMCO was reported at estimated fair value, as determined by a contractual put and call option price, with changes in estimated fair value reported as a component of OCI, net of taxes.

During the year ended December 31, 2008, the Company exercised a put option and sold all of its remaining interest in PIMCO to Allianz of America, Inc., a subsidiary of Allianz SE, for \$288 million. The Company recognized a pre-tax gain of \$109 million for the year ended December 31, 2008.

6. BUSINESS ACQUISITION

On July 18, 2008, Pacific LifeCorp acquired Scottish Re Holdings Limited, its subsidiary Scottish Re Limited, and certain contracts and agreements, which comprised the International Life Reinsurance segment of Scottish Re Group Limited. The new operation does business as Pacific Life Re Limited (Pacific Life Re) and provides reinsurance to insurance and annuity providers in the United Kingdom and Ireland and to insurers in selected markets in Asia. Pacific Life Re's headquarters are located in London with its Asia business being managed from Singapore.

The Company paid cash of \$70 million for the acquisition, including expenses of approximately \$2 million. Concurrent with the acquisition, the Company provided Pacific Life Re with additional capital of \$115 million. The additional capital was contributed to strengthen the financial position and liquidity of Pacific Life Re.

Accounting for business combinations under the Codification's Business Combinations Topic requires that the total purchase price be allocated to the assets acquired and liabilities assumed based on their estimated fair values at the acquisition date. The purchase price allocation process was finalized during the second quarter of 2009 and was not adjusted from the initial assessment.

The following table summarizes the fair values of the net assets acquired (*In Millions*) as of the acquisition date:

Investments	\$243
Reinsurance receivable ⁽¹⁾	102
Fixed assets and leasehold improvements ⁽¹⁾	5
Other assets	12
Future policy benefits	(244)
Reinsurance payables ⁽²⁾	(39)
Accounts payable, accruals and other liabilities ⁽²⁾	(9)
Total net assets acquired	<u>\$70</u>

⁽¹⁾ Included in other assets. ⁽²⁾ Included in other liabilities.

7. DISCONTINUED OPERATIONS

The Company's broker-dealer operations and group insurance business have been reflected as discontinued operations in the Company's consolidated financial statements. Discontinued operations do not include the operations of Pacific Select Distributors, Inc. (PSD), a wholly owned broker-dealer subsidiary of Pacific Life, which primarily serves as the underwriter/distributor of registered investment-related products and services, principally variable life and variable annuity contracts issued by the Company, and mutual funds.

In March 2007, the Company classified its broker-dealer subsidiaries, other than PSD, as held for sale. On June 20, 2007, a transaction closed whereby the Company sold certain of these broker-dealer subsidiaries to an unrelated third-party. Proceeds from the sale included cash of \$53 million and a common stock interest in the buyer's parent of \$57 million. A pre-tax gain of \$54 million was recognized from this sale during the year ended December 31, 2007. On December 31, 2007, a transaction closed whereby the Company sold another one of its broker-dealer subsidiaries to subsidiary management. The Company incurred a pre-

tax loss of \$1 million from this transaction during the year ended December 31, 2007. As of December 31, 2007, one broker-dealer subsidiary remained classified as held for sale. On March 31, 2008, a transaction closed whereby the Company sold this held for sale subsidiary to an unrelated third-party. The Company recognized an insignificant pre-tax gain from this transaction during the year ended December 31, 2008.

Operating results of discontinued operations were as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Revenues		\$13	\$276
Benefits and expenses	\$31	22	300
Loss from discontinued operations	(31)	(9)	(24)
Benefit from income taxes	(11)	(3)	(8)
Loss from discontinued operations, net of taxes	(20)	(6)	(16)
Net gain on sale of discontinued operations			53
Provision for income taxes			26
Net gain on sale of discontinued operations, net of taxes			27
Discontinued operations, net of taxes	(\$20)	(\$6)	\$11

Assets and liabilities from discontinued operations are included in other assets and other liabilities, respectively. Assets related to discontinued operations were zero and \$6 million as of December 31, 2009 and 2008, respectively. Liabilities related to discontinued operations were zero and \$13 million as of December 31, 2009 and 2008, respectively.

8. DEFERRED POLICY ACQUISITION COSTS

Components of DAC are as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Balance, January 1	\$5,028	\$4,481	\$4,248
Cumulative pre-tax effect of adoption of new accounting principle (Note 1)	7		(45)
Additions:			
Capitalized during the year	822	774	852
Amortization:			
Allocated to commission expenses	(457)	(449)	(432)
Allocated to operating expenses	(130)	(133)	(118)
Total amortization	(587)	(582)	(550)
Allocated to OCI	(413)	355	(24)
Balance, December 31	\$4,857	\$5,028	\$4,481

During the years ended December 31, 2009, 2008 and 2007, the Company revised certain assumptions to develop EGPs for its products subject to DAC amortization (Note 1). This resulted in increases in DAC amortization expense of \$23 million and \$20 million for the years ended December 31, 2009 and 2008, respectively, and a decrease in DAC amortization expense of \$12 million for the year ended December 31, 2007. The revised EGPs also resulted in an immaterial decrease in URR amortization for the year ended December 31, 2009, increased URR amortization of \$2 million for the year ended December 31, 2008, and decreased URR amortization of \$15 million for the year ended December 31, 2007.

9. INVESTMENTS

The net carrying amount, gross unrealized gains and losses, and estimated fair value of fixed maturity and equity securities available for sale are shown below. The net carrying amount represents amortized cost adjusted for credit related OTTI and changes in the estimated fair value of fixed maturity securities attributable to the hedged risk in a fair value hedge. See Note 15 for information on the Company's fair value measurement and disclosure.

	Net		Estimated	
	Carrying	Gross Unrealized		Fair Value
	Amount	Gains	Losses	Fair Value
<i>(In Millions)</i>				
<u>December 31, 2009:</u>				
U.S. Treasury securities and obligations of				
U.S. government authorities and agencies	\$119	\$10	\$1	\$128
Obligations of states and political subdivisions	636	13	46	603
Foreign governments	390	42		432
Corporate securities	17,529	908	310	18,127
RMBS	6,479	109	1,083	5,505
Commercial mortgage-backed securities	1,161	43	24	1,180
Collateralized debt obligations	118	27	33	112
Other asset-backed securities	566	46	17	595
Total fixed maturity securities	<u>\$26,998</u>	<u>\$1,198</u>	<u>\$1,514</u>	<u>\$26,682</u>
Perpetual preferred securities	\$356	\$6	\$55	\$307
Other equity securities	65	3		68
Total equity securities	<u>\$421</u>	<u>\$9</u>	<u>\$55</u>	<u>\$375</u>

	Net		Estimated	
	Carrying	Gross Unrealized		Fair Value
	Amount	Gains	Losses	Fair Value
<i>(In Millions)</i>				
<u>December 31, 2008:</u>				
U.S. Treasury securities and obligations of				
U.S. government authorities and agencies	\$103	\$19		\$122
Obligations of states and political subdivisions	512	5	\$148	369
Foreign governments	307	46	7	346
Corporate securities	16,004	312	1,624	14,692
RMBS	6,514	106	1,318	5,302
Commercial mortgage-backed securities	1,193	15	105	1,103
Collateralized debt obligations	126		2	124
Other asset-backed securities	624	32	110	546
Total fixed maturity securities	<u>\$25,383</u>	<u>\$535</u>	<u>\$3,314</u>	<u>\$22,604</u>
Perpetual preferred securities	\$389	\$3	\$175	\$217
Other equity securities	2			2
Total equity securities	<u>\$391</u>	<u>\$3</u>	<u>\$175</u>	<u>\$219</u>

The Company has investments in perpetual preferred securities that are issued primarily by European and U.S. banks. The net carrying amount and estimated fair value of the available for sale perpetual preferred securities was \$483 million and \$423 million, respectively, as of December 31, 2009. Included in these amounts are perpetual preferred securities carried in trusts with a net carrying amount and estimated fair value of \$127 million and \$116 million, respectively, that are held in fixed maturities and included in the tables above in corporate securities. Perpetual preferred securities reported as equity securities available for sale are presented in the tables above as perpetual preferred securities.

The net carrying amount and estimated fair value of fixed maturity securities available for sale as of December 31, 2009, by contractual repayment date of principal, are shown below. Expected maturities may differ from contractual maturities as borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Net Carrying Amount	Gross Unrealized		Estimated Fair Value
		Gains	Losses	
		<i>(In Millions)</i>		
Due in one year or less	\$1,846	\$68	\$25	\$1,889
Due after one year through five years	5,262	289	55	5,496
Due after five years through ten years	7,309	367	135	7,541
Due after ten years	4,257	249	142	4,364
	18,674	973	357	19,290
Mortgage-backed and asset-backed securities	8,324	225	1,157	7,392
Total	\$26,998	\$1,198	\$1,514	\$26,682

The following tables present the number of investments, estimated fair value and gross unrealized losses on investments where the estimated fair value has declined and remained continuously below the net carrying amount for less than twelve months and for twelve months or greater. Included in the tables are gross unrealized losses for fixed maturity securities available for sale and other securities, which include equity securities available for sale, cost method investments, and non-marketable securities.

	Total		
	Number	Estimated Fair Value	Gross Unrealized Losses
<i>(In Millions)</i>			
<u>December 31, 2009:</u>			
U.S. Treasury securities and obligations of			
U.S. government authorities and agencies	7	\$13	\$1
Obligations of states and political subdivisions	27	383	46
Corporate securities	559	4,673	310
RMBS	385	3,998	1,083
Commercial mortgage-backed securities	20	340	24
Collateralized debt obligations	6	61	33
Other asset-backed securities	24	205	17
Total fixed maturity securities	<u>1,028</u>	<u>9,673</u>	<u>1,514</u>
Perpetual preferred securities	18	195	55
Other securities	31	97	26
Total other securities	<u>49</u>	<u>292</u>	<u>81</u>
Total	<u>1,077</u>	<u>\$9,965</u>	<u>\$1,595</u>

	Less than 12 Months			12 Months or Greater		
	Number	Estimated Fair Value	Gross Unrealized Losses	Number	Estimated Fair Value	Gross Unrealized Losses
<i>(In Millions)</i>						
<u>December 31, 2009:</u>						
U.S. Treasury securities and obligations of						
U.S. government authorities and agencies	7	\$13	\$1			
Obligations of states and political subdivisions	11	116	6	16	\$267	\$40
Corporate securities	299	1,900	52	260	2,773	258
RMBS	77	599	96	308	3,399	987
Commercial mortgage-backed securities	6	100	5	14	240	19
Collateralized debt obligations	5	59	32	1	2	1
Other asset-backed securities				24	205	17
Total fixed maturity securities	<u>405</u>	<u>2,787</u>	<u>192</u>	<u>623</u>	<u>6,886</u>	<u>1,322</u>
Perpetual preferred securities				18	195	55
Other securities	16	54	9	15	43	17
Total other securities	<u>16</u>	<u>54</u>	<u>9</u>	<u>33</u>	<u>238</u>	<u>72</u>
Total	<u>421</u>	<u>\$2,841</u>	<u>\$201</u>	<u>656</u>	<u>\$7,124</u>	<u>\$1,394</u>

	Total		
	Number	Gross	
		Estimated Fair Value	Unrealized Losses
<i>(In Millions)</i>			
<u>December 31, 2008:</u>			
Obligations of states and political subdivisions	33	\$279	\$148
Foreign governments	5	66	7
Corporate securities	1,014	9,752	1,624
RMBS	459	3,989	1,318
Commercial mortgage-backed securities	47	798	105
Collateralized debt obligations	5	2	2
Other asset-backed securities	52	333	110
Total fixed maturity securities	<u>1,615</u>	<u>15,219</u>	<u>3,314</u>
Perpetual preferred securities	33	200	175
Other securities	24	95	28
Total other securities	<u>57</u>	<u>295</u>	<u>203</u>
Total	<u>1,672</u>	<u>\$15,514</u>	<u>\$3,517</u>

	Less than 12 Months			12 Months or Greater		
	Number	Gross		Number	Gross	
		Estimated Fair Value	Unrealized Losses		Estimated Fair Value	Unrealized Losses
<i>(In Millions)</i>						
<u>December 31, 2008:</u>						
Obligations of states and political subdivisions	30	\$257	\$144	3	\$22	\$4
Foreign governments	5	66	7			
Corporate securities	709	6,756	809	305	2,996	815
RMBS	198	2,436	707	261	1,553	611
Commercial mortgage-backed securities	33	571	73	14	227	32
Collateralized debt obligations	4	1	2	1	1	
Other asset-backed securities	34	210	48	18	123	62
Total fixed maturity securities	<u>1,013</u>	<u>10,297</u>	<u>1,790</u>	<u>602</u>	<u>4,922</u>	<u>1,524</u>
Perpetual preferred securities	10	32	17	23	168	158
Other securities	18	89	27	6	6	1
Total other securities	<u>28</u>	<u>121</u>	<u>44</u>	<u>29</u>	<u>174</u>	<u>159</u>
Total	<u>1,041</u>	<u>\$10,418</u>	<u>\$1,834</u>	<u>631</u>	<u>\$5,096</u>	<u>\$1,683</u>

The Company has evaluated fixed maturity and other securities with gross unrealized losses and determined that the unrealized losses are temporary and that the Company does not intend to sell the securities and it is more likely than not that the Company will not be required to sell the securities before recovery of their net carrying amounts.

Prime mortgages are loans made to borrowers with strong credit histories, whereas sub-prime mortgage lending is the origination of residential mortgage loans to customers with weak credit profiles. Alt-A mortgage lending is the origination of residential mortgage loans to customers who have good credit ratings, but have limited documentation for their source of income or some other standard input used to underwrite the mortgage loan. The slowing U.S. housing market, greater use of affordability mortgage

products and relaxed underwriting standards by some originators for these loans has led to higher delinquency and loss rates, especially within the 2007 and 2006 vintage years.

The table below illustrates the breakdown of non-agency RMBS and commercial mortgage-backed securities (CMBS) by investment rating from independent rating agencies and vintage year of the underlying collateral as of December 31, 2009.

Rating	Net Carrying Amount	Estimated Fair Value	Rating as % of Net Carrying Amount	Vintage Breakdown					
				2004 and Prior	2005	2006	2007	2008	2009
(\$ In Millions)									
Prime RMBS:									
AAA	\$1,049	\$966	31%	23%	7%	1%			
AA	323	281	9%	4%	2%	3%			
A	259	214	8%	1%	2%	3%	2%		
BAA	527	405	15%	2%	7%	6%			
BA and below	1,264	893	37%		8%	17%	12%		
Total	\$3,422	\$2,759	100%	30%	26%	30%	14%	0%	0%
Alt-A RMBS:									
AAA	\$64	\$57	6%	6%					
AA	17	21	2%	2%					
A	13	10	1%	1%					
BAA	25	23	3%		1%	2%			
BA and below	844	556	88%		10%	27%	51%		
Total	\$963	\$667	100%	9%	11%	29%	51%	0%	0%
Sub-prime RMBS:									
AAA	\$231	\$180	52%	52%					
AA	98	73	22%	22%					
A	21	13	5%	5%					
BAA	42	33	9%		9%				
BA and below	53	37	12%	1%	9%	1%	1%		
Total	\$445	\$336	100%	80%	18%	1%	1%	0%	0%
CMBS:									
AAA	\$1,017	\$1,054	88%	65%	3%		15%	1%	4%
AA	67	62	6%	4%					2%
A	37	32	3%	3%					
BAA	28	22	2%				2%		
BA	12	10	1%	1%					
Total	\$1,161	\$1,180	100%	73%	3%	0%	17%	1%	6%

As of December 31, 2009, the Company has received advances of \$1.5 billion from the Federal Home Loan Bank (FHLB) of Topeka and has issued funding agreements to the FHLB of Topeka. Funding agreements are used as an alternative source of funds for the Company's spread lending business and the funding agreement liabilities are included in general account policyholder account balances. Assets with an estimated fair value of \$1.8 billion as of December 31, 2009 are in a custodial account pledged as collateral for the funding agreements. The Company is required to purchase stock in FHLB of Topeka each time it receives an advance. As of December 31, 2009, the Company holds \$76 million of FHLB of Topeka stock.

PL&A is a member of FHLB of San Francisco. As of December 31, 2009, no assets are pledged as collateral. As of December 31, 2009, the Company holds \$25 million of FHLB of San Francisco stock.

The Company had a securities lending program administered by one of the largest U.S. financial institutions specializing in securities lending and short-term fixed-income asset management. This securities lending program was terminated in February 2009. Securities loaned were zero as of December 31, 2008.

Major categories of investment income and related investment expense are summarized as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Fixed maturity securities	\$1,477	\$1,489	\$1,518
Equity securities	20	23	26
Mortgage loans	297	289	248
Real estate	94	87	69
Policy loans	229	223	209
Partnerships and joint ventures	(77)	21	179
Other	16	34	47
Gross investment income	2,056	2,166	2,296
Investment expense	159	137	139
Net investment income	\$1,897	\$2,029	\$2,157

The components of net realized investment gain (loss) are as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Fixed maturity securities:			
Gross gains on sales	\$54	\$106	\$117
Gross losses on sales	(19)	(44)	(23)
Other	12	4	20
Total fixed maturity securities	47	66	114
Equity securities:			
Gross gains on sales			5
Gross losses on sales	(11)		
Other	2	1	
Total equity securities	(9)	1	5
Trading securities	20	(22)	(1)
Variable annuity GLB embedded derivatives	2,211	(2,775)	(222)
Variable annuity GLB policy fees	147	108	78
Variable annuity derivatives - interest rate swaps	(104)	402	
Variable annuity derivatives - total return swaps	(1,542)	646	13
Equity put options	(672)	853	31
Synthetic GIC policy fees	25	15	
Other derivatives	38	(78)	(11)
Other	3	17	63
Total	\$164	(\$767)	\$70

As a result of the significant disruption in the housing, financial and credit markets, the OTTI charges recorded during the year ended December 31, 2009 were primarily related to the Company's exposure to RMBS, certain structured securities and direct exposure to corporate securities. The table below summarizes the OTTIs by security type (*In Millions*):

	Recorded in Earnings	Included in OCI	Total
<u>Year ended December 31, 2009:</u>			
Corporate securities	\$63 ⁽¹⁾	\$2	\$65
RMBS	117	315	432
Collateralized debt obligations	66	13	79
Perpetual preferred securities	26		26
Other investments	40		40
Total OTTIs	<u>\$312</u>	<u>\$330</u>	<u>\$642</u>
<u>Year ended December 31, 2008:</u>			
Corporate securities	\$74		
RMBS	227		
Collateralized debt obligations	156		
Other asset-backed securities	1		
Perpetual preferred securities	68		
Other equity securities	58		
Total OTTIs	<u>\$584</u>		

(1) Included are \$29 million of OTTI recorded in earnings on perpetual preferred securities carried in trusts.

In accordance with additional guidance under the Codification's Investments – Debt and Equity Securities Topic effective January 1, 2009, the Company began recording the credit loss portion of OTTI adjustments in earnings and the portion related to other factors in OCI. The table below details the amount of OTTIs attributable to credit losses recorded in earnings for which a portion was recognized in OCI (*In Millions*):

Cumulative credit loss, January 1, 2009	\$88
Additions for credit impairments recognized on:	
Securities not previously other than temporarily impaired	48
Securities previously other than temporarily impaired	106
Total additions	<u>154</u>
Reductions for credit impairments previously recognized on:	
Securities that matured or were sold	(40)
Securities due to an increase in expected cash flows and time value of cash flows	(2)
Total subtractions	<u>(42)</u>
Cumulative credit loss, December 31, 2009	<u>\$200</u>

The table below presents separately the gross unrealized losses on investments for which OTTI has been recorded in earnings in current or prior periods and the gross unrealized losses on temporarily impaired investments for which no OTTI has been recorded.

	Gross Unrealized Losses		
	OTTI	Non-OTTI	Total
	Investments	Investments	
	<i>(In Millions)</i>		
<u>December 31, 2009:</u>			
U.S. Treasury securities and obligations of U.S. government authorities and agencies		\$1	\$1
Obligations of states and political subdivisions		46	46
Corporate securities	\$2	308	310
RMBS	328	755	1,083
CMBS		24	24
Collateralized debt obligations	32	1	33
Other asset-backed securities		17	17
Total fixed maturity securities	<u>\$362</u>	<u>\$1,152</u>	<u>\$1,514</u>
Perpetual preferred securities		\$55	\$55
Total equity securities		<u>\$55</u>	<u>\$55</u>

The change in unrealized gain (loss) on investments in available for sale and trading securities is as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Available for sale securities:			
Fixed maturity	\$2,463	(\$3,273)	(\$204)
Equity	126	(144)	(49)
Total available for sale securities	<u>\$2,589</u>	<u>(\$3,417)</u>	<u>(\$253)</u>
Trading securities	<u>\$26</u>	<u>(\$19)</u>	<u>(\$2)</u>

Trading securities totaled \$206 million and \$114 million as of December 31, 2009 and 2008, respectively. The cumulative unrealized gains (losses) on trading securities held as of December 31, 2009 and 2008 were \$7 million and (\$19) million, respectively.

As of December 31, 2009 and 2008, fixed maturity securities of \$12 million were on deposit with state insurance departments to satisfy regulatory requirements.

Mortgage loans totaled \$6,577 million and \$5,622 million as of December 31, 2009 and 2008, respectively. Mortgage loans are collateralized by commercial real estate properties primarily located throughout the U.S. As of December 31, 2009, \$1,122 million, \$963 million, \$785 million, \$554 million and \$369 million were located in California, Washington, Florida, Texas and Maryland, respectively. As of December 31, 2009, \$543 million was located in Canada. There were no defaults during the years ended December 31, 2009, 2008, and 2007. The Company did not have any mortgage loans with accrued interest more than 180 days past due as of December 31, 2009 or 2008. As of December 31, 2009, mortgage loan investments with one commercial sponsor exceeded 10% of stockholder's equity. The carrying value of these investments was \$725 million as of December 31, 2009.

Investments in real estate totaled \$583 million and \$468 million as of December 31, 2009 and 2008, respectively. There were no real estate write-downs during the years ended December 31, 2009, 2008 and 2007.

10. AIRCRAFT LEASING PORTFOLIO, NET

Aircraft leasing portfolio, net, consisted of the following:

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Aircraft consolidated from VIEs	\$3,081	\$3,099
Other aircraft	3,217	2,667
	<u>6,298</u>	<u>5,766</u>
Accumulated depreciation	994	767
Aircraft leasing portfolio, net	<u>\$5,304</u>	<u>\$4,999</u>

As of December 31, 2009, domestic and foreign future minimum rentals scheduled to be received under the noncancelable portion of operating leases are as follows *(In Millions)*:

	2010	2011	2012	2013	2014	Thereafter
Domestic	\$23	\$19	\$15	\$13	\$13	\$28
Foreign	526	448	369	274	214	390
Total operating leases	<u>\$549</u>	<u>\$467</u>	<u>\$384</u>	<u>\$287</u>	<u>\$227</u>	<u>\$418</u>

As of December 31, 2009 and 2008, aircraft with a carrying amount of \$4,954 million and \$4,366 million, respectively, were assigned as collateral to secure debt (Notes 4 and 14).

There were no impairments recorded during the years ended December 31, 2009, 2008 and 2007.

During the years ended December 31, 2009, 2008 and 2007, ACG recognized pre-tax gains on the sale of aircraft of zero, zero and \$18 million, respectively, which are included in other income.

In December 2007, ACG sold its entire ownership interest in an unconsolidated affiliate. The transaction resulted in a pre-tax gain of \$17 million, which is included in net realized investment gain (loss) for the year ended December 31, 2007.

11. DERIVATIVES AND HEDGING ACTIVITIES

The Company primarily utilizes derivative instruments to manage its exposure to interest rate risk, foreign currency risk, credit risk, and equity risk. Derivative instruments are also used to manage the duration mismatch of assets and liabilities. The Company utilizes a variety of derivative instruments including swaps, foreign exchange forward contracts, caps, floors and options. In addition, certain insurance products offered by the Company contain features that are accounted for as derivatives.

Accounting for derivatives and hedging activities requires companies to recognize all derivative instruments as either assets or liabilities at fair value in the consolidated statements of financial condition. In accordance with accounting for derivatives and hedging activities, the Company applies hedge accounting by designating derivative instruments as either fair value or cash flow hedges on the date the Company enters into a derivative contract. The Company formally documents at inception all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategy for undertaking various hedge transactions. In this documentation, the Company specifically identifies the asset, liability, firm commitment, or forecasted transaction that has been designated as a hedged item and states how the hedging instrument is expected to hedge the risks related to the hedged item. The Company formally assesses and measures effectiveness of its hedging relationships both at the hedge inception and on an ongoing basis in accordance with its risk management policy.

DERIVATIVES DESIGNATED AS CASH FLOW HEDGES

The Company primarily uses foreign currency interest rate swaps, forward starting interest rate swaps and interest rate swaps to manage its exposure to variability in cash flows due to changes in foreign currencies and the benchmark interest rate. These cash flows include those associated with existing assets and liabilities, as well as the forecasted interest cash flows related to anticipated investment purchases and liability issuances. Such anticipated investment purchases and liability issuances are considered probable to occur and are generally completed within 22 years of the inception of the hedge.

Foreign currency interest rate swap agreements are used to convert a fixed or floating rate, foreign-denominated asset or liability to a U.S. dollar fixed rate asset or liability. The foreign currency interest rate swaps involve the exchange of an initial principal amount in two currencies, and the agreement to re-exchange the currencies at a future date at an agreed exchange rate. There are also periodic exchanges of interest payments in the two currencies at specified intervals, calculated using agreed upon rates and the exchanged principal amounts. The main currencies that the Company hedges are the Euro, British Pound, and Canadian Dollar.

Forward starting interest rate swaps are used to hedge the variability in the future interest receipts or payments stemming from the anticipated purchase of fixed rate securities or issuance of fixed rate liabilities due to changes in benchmark interest rates. These derivatives are predominantly used to lock in interest rate levels to match future cash flow characteristics of assets and liabilities. Forward starting interest rate swaps involve the exchange, at specified intervals, of interest payments resulting from the difference between fixed and floating rate interest amounts calculated by reference to an underlying notional amount to begin at a specified date in the future for a specified period of time. Generally, no cash is exchanged at the outset of the contract and no principal payments are made by either party. The notional amounts of the contracts do not represent future cash requirements, as the Company intends to close out open positions prior to their effective dates.

Interest rate swap agreements are used to convert a floating rate asset or liability to a fixed rate to hedge the variability of cash flows of the hedged asset or liability due to changes in benchmark interest rates. These derivatives are predominantly used to better match the cash flow characteristics of certain assets and liabilities. These agreements involve the exchange, at specified intervals, of interest payments resulting from the difference between fixed rate and floating rate interest amounts calculated by reference to an underlying notional amount. Generally, no cash is exchanged at the outset of the contract and no principal payments are made by either party.

When a derivative is designated as a cash flow hedge, the effective portion of changes in the estimated fair value of the derivative is recorded in OCI and recognized in earnings when the hedged item affects earnings, and the ineffective portion of changes in the estimated fair value of the derivative is recorded in net realized investment gain (loss). For the years ended December 31, 2009, 2008 and 2007, the Company had net losses of zero, zero and \$21 million, respectively, reclassified from accumulated other comprehensive income (AOCI) to earnings resulting from the discontinuance of cash flow hedges due to forecasted transactions that were no longer probable of occurring. Over the next twelve months, the Company anticipates that \$24 million of deferred losses on derivative instruments in AOCI will be reclassified to earnings. For the years ended December 31, 2009, 2008 and 2007, all of the Company's hedged forecasted transactions were determined to be probable of occurring.

The Company had the following outstanding derivatives designated as cash flow hedges:

	Notional Amount	
	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Foreign currency interest rate swaps	\$5,099	\$6,488
Forward starting interest rate swaps	1,060	1,535
Interest rate swaps	3,910	4,384

Notional amount represents a standard of measurement of the volume of derivatives. Notional amount is not a quantification of market risk or credit risk and is not recorded on the consolidated statements of financial condition. Notional amounts generally represent those amounts used to calculate contractual cash flows to be exchanged and are not paid or received, except for certain contracts such as currency swaps.

DERIVATIVES DESIGNATED AS FAIR VALUE HEDGES

Interest rate swap agreements are used to convert a fixed rate asset or liability to a floating rate to hedge the changes in estimated fair value of the hedged asset or liability due to changes in benchmark interest rates. These derivatives are used primarily to closely match the duration of the assets supporting specific liabilities.

When a derivative is designated as a fair value hedge, the changes in the estimated fair value of the derivative and the hedged item are recognized in net realized investment gain (loss). The change in value of the hedged item associated with the risk being hedged is reflected as an adjustment to the carrying amount of the hedged item. For the years ended December 31, 2009, 2008 and 2007, hedge ineffectiveness related to designated fair value hedges reflected in net realized investment gain (loss) was \$5 million, (\$1) million and zero, respectively. No component of the hedging instrument's estimated fair value is excluded from the determination of effectiveness.

The Company had the following outstanding derivatives designated as fair value hedges:

	Notional Amount	
	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Foreign currency interest rate swaps	\$13	\$18
Interest rate swaps	1,658	1,264

DERIVATIVES NOT DESIGNATED AS HEDGING INSTRUMENTS

The Company has certain insurance and reinsurance contracts that are considered to have embedded derivatives. When it is determined that the embedded derivative possesses economic and risk characteristics that are not clearly and closely related to those of the host contract and that a separate instrument with the same terms would qualify as a derivative instrument, it is separated from the host contract and accounted for as a stand-alone derivative. The changes in the estimated fair value of the derivatives not designated as hedging instruments and the periodic cash flows are recognized in net realized investment gain (loss).

The Company offers a rider on certain variable annuity contracts that guarantees net principal over a ten-year holding period, as well as riders on certain variable annuity contracts that guarantee a minimum withdrawal benefit over specified periods, subject to certain restrictions. These variable annuity GLBs are considered embedded derivatives and are recorded in future policy benefits.

GLBs on variable annuity contracts issued between January 1, 2007 and March 31, 2009 are partially covered by reinsurance. These reinsurance arrangements are used to offset a portion of the Company's exposure to the GLBs for the lives of the host variable annuity contracts issued. The ceded portion of the GLBs is considered an embedded derivative and is recorded in other assets or other liabilities as either a reinsurance recoverable or reinsurance payable.

The Company employs hedging strategies (variable annuity derivatives) to mitigate equity risk associated with the GLBs not covered by reinsurance. The Company utilizes total return swaps based upon the S&P 500 Index (S&P 500) primarily to economically hedge the equity risk of the mortality and expense fees in its variable annuity products. These contracts provide periodic payments to the Company in exchange for the total return of the S&P 500 in the form of a payment or receipt, depending on whether the return relative to the index on trade date is positive or negative, respectively. Payments are recognized in realized investment loss and receipts are recognized in realized investment gain. The Company has used interest rate swaps to hedge fluctuations in the valuation of GLBs as a result of changes in risk free rates. These agreements involved the exchange, at specified intervals, of interest payments resulting from the difference between fixed rate and floating rate interest amounts calculated by reference to an underlying notional amount.

The Company also uses equity put options to hedge equity and credit risks. These equity put options involve the exchange of periodic fixed rate payments for the return, at the end of the option agreement, of the equity index below a specified strike price. Generally, no cash is exchanged at the outset of the contract and no principal payments are made by either party.

The Company offers equity indexed universal life insurance products, which credits the total return of the S&P 500 to the policy cash value. A policyholder may allocate the policy's net accumulated value to one or a combination of the following: fixed return account, one year indexed account capped at 12%, or a five year indexed account.

The Company utilizes one year European style S&P 500 call options to hedge the annual exposure of the indexed life insurance product's index growth rate for the one year indexed account. The Company also purchases five year European style S&P 500 Asian call options to hedge the five year exposure of the indexed life insurance product's index growth rate for the five year indexed account.

The Company issues synthetic GICs to Employee Retirement Income Security Act of 1974 (ERISA) qualified defined contribution employee benefit plans (ERISA Plan). The ERISA Plan uses the contracts in its stable value fixed income option. The Company receives a fee for providing book value accounting for the ERISA Plan stable value fixed income option. The Company does not manage the assets underlying synthetic GICs. In the event that plan participant elections exceed the estimated fair value of the assets or if the contract is terminated and at the end of the termination period the book value under the contract exceeds the estimated fair value of the assets, then the Company is required to pay the ERISA Plan the difference between book value and estimated fair value. The Company mitigates the investment risk through pre-approval and monitoring of the investment guidelines, requiring high quality investments and adjustments to the plan crediting rates to compensate for unrealized losses in the portfolios.

The Company uses credit default swaps in combination with cash instruments to reproduce the investment characteristics of certain investments. Credit default swaps involve the receipt or payment of fixed amounts at specific intervals in exchange for the assumption of or protection from potential credit events associated with the underlying security. The Company writes credit default swaps for which a payment is delivered if the underlying security of the derivative defaults. The maximum potential amounts of future payments under credit default swaps were \$50 million and \$106 million as of December 31, 2009 and 2008, respectively. As of December 31, 2009 and 2008, the fair value of credit derivatives sold by the Company was (\$17) million and (\$41) million, respectively. The terms for these instruments range from one to seven years.

The Company had the following outstanding derivatives not designated as hedging instruments:

	Notional Amount	
	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Variable annuity GLB embedded derivatives	\$36,408	\$33,455
Variable annuity derivatives - interest rate swaps		2,150
Variable annuity derivatives - total return swaps	4,456	2,437
Variable annuity GLB reinsurance contracts	14,878	13,274
Equity put options	5,267	5,173
Synthetic GICs	23,993	23,856
Interest rate swaps	2,438	3,317
Foreign currency interest rate swaps	398	460
Other	1,178	910

CONSOLIDATED FINANCIAL STATEMENT IMPACT

Derivative instruments are recorded in the Company's consolidated statements of financial condition at fair value and are presented as assets or liabilities determined by calculating the net position for each derivative counterparty by legal entity, taking into account income accruals and net cash collateral.

The following table summarizes the gross asset or liability derivative fair value and excludes the impact of offsetting asset and liability positions held with the same counterparty, cash collateral payables and receivables and income accruals. See Note 15.

	Asset Derivatives		Liability Derivatives	
	Estimated Fair Value		Estimated Fair Value	
	December 31,		December 31,	
	2009	2008	2009	2008
	<i>(In Millions)</i>		<i>(In Millions)</i>	
Derivatives designated as hedging instruments:				
Foreign currency interest rate swaps	\$177	\$308 ⁽¹⁾	\$230	\$87 ⁽¹⁾
	69	146 ⁽⁵⁾	153	423 ⁽⁵⁾
Forward starting interest rate swap agreements	34	88 ⁽¹⁾		23 ⁽¹⁾
	8	232 ⁽⁵⁾		45 ⁽⁵⁾
Interest rate swaps	34	32 ⁽¹⁾	122	219 ⁽¹⁾
	74	72 ⁽⁵⁾	196	240 ⁽⁵⁾
Total derivatives designated as hedging instruments	<u>396</u>	<u>878</u>	<u>701</u>	<u>1,037</u>
Derivatives not designated as hedging instruments:				
Variable annuity derivatives - interest rate swaps		232 ⁽¹⁾		
		140 ⁽⁵⁾		
Variable annuity derivatives - total return swaps	6	⁽¹⁾	60	33 ⁽¹⁾
		55 ⁽⁵⁾	4	53 ⁽⁵⁾
Equity put options	329	350 ⁽¹⁾	16	⁽¹⁾
	41	587 ⁽⁵⁾	14	⁽⁵⁾
Foreign currency interest rate swaps	21	1 ⁽¹⁾		
		15 ⁽⁵⁾		13 ⁽⁵⁾
Interest rate swaps	39	68 ⁽¹⁾	24	11 ⁽¹⁾
	1	11 ⁽⁵⁾	43	133 ⁽⁵⁾
Other	19	2 ⁽¹⁾	23	1 ⁽¹⁾
	26	12 ⁽⁵⁾		40 ⁽⁵⁾
Embedded derivatives:				
Variable annuity GLB embedded derivatives (including reinsurance contracts)	52	429 ⁽²⁾	754	3,342 ⁽³⁾
Synthetic GICs				3 ⁽³⁾
Other			45	8 ⁽⁴⁾
Total derivatives not designated as hedging instruments	<u>534</u>	<u>1,902</u>	<u>983</u>	<u>3,637</u>
Total derivatives	<u>\$930</u>	<u>\$2,780</u>	<u>\$1,684</u>	<u>\$4,674</u>

Location on the consolidated statements of financial condition:

⁽¹⁾ Other investments ⁽²⁾ Other assets ⁽³⁾ Future policy benefits ⁽⁴⁾ Policyholder account balances ⁽⁵⁾ Other liabilities

Net cash collateral received from counterparties was \$237 million and \$1,392 million as of December 31, 2009 and 2008, respectively. This unrestricted cash collateral is included in cash and cash equivalents and the obligation to return it is netted against the estimated fair value of derivatives in other investments or other liabilities. Net cash collateral pledged to counterparties was \$181 million and \$93 million as of December 31, 2009 and 2008, respectively. A receivable representing the right to call this collateral back from the counterparty is netted against the estimated fair value of derivatives in other investments or other liabilities. If the net estimated fair value exposure to the counterparty is positive, the amount is reflected in other investments, whereas, if the net estimated fair value exposure to the counterparty is negative, the estimated fair value is included in future policy benefits or other liabilities, depending on the nature of the derivative.

As of December 31, 2009 and 2008, the Company had also accepted collateral consisting of various securities with an estimated fair value of \$26 million and \$163 million, respectively, which are held in separate custodial accounts. The Company is permitted by contract to sell or repledge this collateral and as of December 31, 2009 and 2008, \$1 million and \$15 million, respectively, of the collateral had been repledged. As of December 31, 2009 and 2008, the Company provided collateral in the form of various securities of zero and \$17 million, respectively, which are included in fixed maturity securities. The counterparties are permitted by contract to sell or repledge this collateral.

The following table summarizes amounts recorded in net realized investment gain (loss) for derivatives designated as fair value hedges. Gains and losses include the changes in estimated fair value of the derivatives and the hedged items, and amounts realized on terminations. The net of the amounts presented for each year represent the ineffective portion of the hedge. The amounts presented do not include the periodic net coupon settlements of the derivatives or the coupon income (expense) related to the hedged item.

	Gain (Loss) Recognized in Income on Derivatives			Gain (Loss) Recognized in Income on Hedged Items		
	Years Ended			Years Ended		
	December 31,			December 31,		
	2009	2008	2007	2009	2008	2007
	<i>(In Millions)</i>			<i>(In Millions)</i>		
Derivatives in fair value hedges:						
Foreign currency interest rate swaps		(\$1)	(\$1)	\$1	\$2	
Interest rate swaps	\$97	(102)	(32)	(\$93)	101	32
Total	\$97	(\$103)	(\$33)	(\$93)	\$102	\$34

The following table summarizes amounts recorded in the consolidated financial statements for derivatives designated as cash flow hedges. Gain and losses include the changes in estimated fair value of the derivatives and amounts realized on terminations. The amounts presented do not include the periodic net coupon settlements of the derivatives.

	Gain (Loss) Recognized in OCI on Derivatives (Effective Portion)			Gain (Loss) Reclassified from AOCI into Income (Effective Portion)			Gain (Loss) Recognized in Income on Derivatives (Ineffective Portion)				
	Years Ended			Years Ended			Years Ended				
	December 31,			December 31,			December 31,				
	2009	2008	2007	2009	2008	2007	2009	2008	2007		
<i>(In Millions)</i>			<i>(In Millions)</i>			<i>(In Millions)</i>					
Derivatives in cash flow hedges:											
Foreign currency interest rate swaps	\$42	\$67	(\$97)	(\$104)	(\$368)	(\$3)	⁽¹⁾		\$1	⁽¹⁾	
				9	14	18	⁽³⁾				
Forward starting interest rate swaps	(254)	336	32		4		⁽¹⁾	(\$1)	\$3	(2)	⁽¹⁾
						(1)	⁽²⁾				
Interest rate swaps	71	(145)	(84)	(11)	(1)	(1)	⁽³⁾				
				9		(1)	⁽¹⁾	9	(7)		⁽¹⁾
				(1)			⁽²⁾				
Futures				(18)		(3)	⁽³⁾				
				1	3	4	⁽²⁾				
					(1)	(1)	⁽³⁾				
Total	(\$141)	\$258	(\$149)	(\$115)	(\$349)	\$12		\$8	(\$4)	(\$1)	

Location on the consolidated statements of operations:

⁽¹⁾Net realized investment gain (loss) ⁽²⁾Net investment income ⁽³⁾Interest credited to policyholder account balances

The following table summarizes amounts recorded in the consolidated financial statements for derivatives not designated as hedging instruments. Gains and losses include the changes in estimated fair value of the derivatives and amounts realized on terminations. The amounts presented do not include the periodic net coupon settlements of (\$1,485) million, \$639 million and (\$41) million for the years ended December 31, 2009, 2008 and 2007, respectively, which are recorded in net realized investment gain (loss).

	Amount of Gain (Loss)		
	Recognized in		
	Income on Derivatives		
	Years Ended		
	December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Derivatives not designated as hedging instruments:			
Variable annuity derivatives - interest rate swaps	(\$168)	\$386	(1)
Variable annuity derivatives - total return swaps	(102)	(55)	\$28 (1)
Equity put options	(580)	927	55 (1)
Foreign currency interest rate swaps	(8)	12	(2) (1)
	(1)	(1)	(2)
Interest rate swaps	4	(18)	3 (1)
	(1)	(9)	(2)
Other	42	(61)	(1)
Embedded derivatives:			
Variable annuity GLB embedded derivatives (including reinsurance contracts)	2,211	(2,775)	(222) (1)
Other embedded derivatives	(14)	13	1 (1)
Total	\$1,383	(\$1,581)	(\$137)

Location on the consolidated statements of operations:

(1) Net realized investment gain (loss) (2) Interest credited to policyholder account balances

CREDIT EXPOSURE AND CREDIT RISK RELATED CONTINGENT FEATURES

Credit exposure is measured on a counterparty basis as the net positive aggregate estimated fair value, net of collateral received, if any. The credit exposure for over the counter derivatives as of December 31, 2009 was \$137 million. The maximum exposure to any single counterparty was \$41 million at December 31, 2009.

For all derivative contracts, excluding embedded derivative contracts such as variable annuity GLBs and synthetic GICs, the Company enters into master agreements that may include a termination event clause associated with Pacific Life's insurer financial strength ratings assigned by certain independent rating agencies. If Pacific Life's insurer financial strength rating falls below a specified level, as defined within each counterparty master agreement or, in most cases, if one of the rating agencies ceases to provide an insurer financial strength rating, the counterparty can terminate the master agreement with payment due based on the estimated fair value of the underlying derivatives. As of December 31, 2009, Pacific Life's insurer financial strength ratings were above the specified level.

If Pacific Life's insurer financial strength rating were to fall below the next investment grade from its current standing, the counterparties to the derivative instruments could request immediate and ongoing full overnight collateralization on derivative instruments in net liability positions. The aggregate fair value of all derivative instruments with credit risk related contingent features that are in a liability position on December 31, 2009, is \$338 million for which the Company has posted collateral of \$182 million in the normal course of business. If certain of Pacific Life's insurer financial strength ratings were to fall one notch as of December 31, 2009, the Company would have been required to post an additional \$14 million of collateral to its counterparties.

The Company attempts to limit its credit exposure by dealing with creditworthy counterparties, establishing risk control limits, executing legally enforceable master netting agreements, and obtaining collateral where appropriate. In addition, each counterparty is reviewed to evaluate its financial stability before entering into each agreement and throughout the period that the financial instrument is owned. All of the Company's credit exposure from derivative contracts is with investment grade

counterparties. For the year ended December 31, 2009, the Company has incurred losses of \$4 million, included in net realized investment gain (loss), on derivative instruments due to counterparty default related to the bankruptcy of Lehman Brothers Special Finance. These losses were a result of the termination of all remaining open positions with Lehman counterparties.

12. POLICYHOLDER LIABILITIES

POLICYHOLDER ACCOUNT BALANCES

The detail of the liability for policyholder account balances is as follows:

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Universal life	\$19,298	\$18,729
Annuity and deposit liabilities	7,109	4,515
Funding agreements	5,240	7,890
GICs	2,337	1,536
Total	<u>\$33,984</u>	<u>\$32,670</u>

FUTURE POLICY BENEFITS

The detail of the liability for future policy benefits is as follows:

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Annuity reserves	\$4,960	\$4,506
Variable annuity GLB embedded derivatives	754	3,342
URR	734	928
Life insurance	618	390
Policy benefits payable	342	456
Closed Block liabilities	306	311
Other	24	174
Total	<u>\$7,738</u>	<u>\$10,107</u>

13. SEPARATE ACCOUNTS AND VARIABLE ANNUITY GUARANTEED BENEFIT FEATURES

The Company issues variable annuity contracts through separate accounts for which investment income and investment gains and losses accrue directly to, and investment risk is borne by, the contract holder (traditional variable annuities). These contracts also include various types of guaranteed minimum death benefit (GMDB) and GLB features. For a discussion of certain GLBs accounted for as embedded derivatives, see Note 11.

The GMDBs provide a specified minimum return upon death. Many of these death benefits are spousal, whereby a death benefit will be paid upon death of the first spouse. The survivor has the option to terminate the contract or continue it and have the death benefit paid into the contract and a second death benefit paid upon the survivor's death. The GMDB features include those where the Company contractually guarantees to the contract holder either (a) return of no less than total deposits made to the contract less any partial withdrawals (return of net deposits), (b) the highest contract value on any contract anniversary date through age 80 minus any payments or withdrawals following the contract anniversary (anniversary contract value), or (c) the highest of contract value on certain specified dates or total deposits made to the contract less any partial withdrawals plus a minimum return (minimum return).

The guaranteed minimum income benefit (GMIB) is a GLB that provides the contract holder with a guaranteed annuitization value after 10 years. Annuitization value is generally based on deposits adjusted for withdrawals plus a minimum return. In general, the GMIB requires contract holders to invest in an approved asset allocation strategy.

Information in the event of death on the various GMDB features outstanding was as follows (the Company's variable annuity contracts with guarantees may offer more than one type of guarantee in each contract; therefore, the amounts listed are not mutually exclusive):

	December 31,	
	2009	2008
	<i>(\$ In Millions)</i>	
Return of net deposits		
Separate account value	\$46,884	\$36,672
Net amount at risk ⁽¹⁾	4,017	11,557
Average attained age of contract holders	61 years	61 years
Anniversary contract value		
Separate account value	\$16,483	\$13,465
Net amount at risk ⁽¹⁾	2,541	5,750
Average attained age of contract holders	63 years	62 years
Minimum return		
Separate account value	\$1,241	\$1,107
Net amount at risk ⁽¹⁾	620	898
Average attained age of contract holders	65 years	64 years

⁽¹⁾ Represents the amount of death benefit in excess of the current account balance as of December 31.

Information regarding GMIB features outstanding is as follows:

	December 31,	
	2009	2008
	<i>(\$ In Millions)</i>	
Separate account value	\$2,675	\$2,230
Average attained age of contract holders	58 years	57 years

The determination of GMDB and GMIB liabilities is based on models that involve a range of scenarios and assumptions, including those regarding expected market rates of return and volatility, contract surrender rates and mortality experience. The following table summarizes the GMDB and GMIB liabilities, which are recorded in future policy benefits, and changes in these liabilities, which are reflected in policy benefits paid or provided:

	December 31,		December 31,	
	2009	2008	2009	2008
	GMDB		GMIB	
	<i>(In Millions)</i>		<i>(In Millions)</i>	
Balance, beginning of year	\$119	\$48	\$62	\$24
Changes in reserves	(11)	119	(23)	38
Benefits paid	(108)	(48)	(1)	
Balance, end of year	<u>\$0</u>	<u>\$119</u>	<u>\$38</u>	<u>\$62</u>

Reinsurance recoverables related to GMDB reserves totaled zero and \$3 million as of December 31, 2009 and 2008, respectively, which are included with other reinsurance receivables in other assets. Reinsurance recoverables related to GMIB reserves are not significant.

Variable annuity contracts with guarantees were invested in separate account investment options as follows:

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Asset type		
Domestic equity	\$25,760	\$17,927
International equity	6,728	5,476
Bonds	13,775	12,182
Money market	621	1,087
Total separate account value	<u>\$46,884</u>	<u>\$36,672</u>

14. DEBT

Debt consists of the following:

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Short-term debt:		
Revolving credit facilities	\$220	\$315
Credit facility recourse only to ACG	105	150
CSB repurchase agreements	214	195
Other		139
Total short-term debt	<u>\$539</u>	<u>\$799</u>
Long-term debt:		
Surplus notes	\$1,150	\$150
Senior notes	600	600
Fair value adjustment and deferred gains for derivatives and hedging activities	264	339
Non-recourse long-term debt:		
Debt recourse only to ACG	1,636	1,271
ACG non-recourse debt	761	687
Other non-recourse debt	121	121
ACG VIE debt (Note 4)	1,975	2,173
Other VIE debt (Note 4)	2	2
Total long-term debt	<u>\$6,509</u>	<u>\$5,343</u>

SHORT-TERM DEBT

Pacific LifeCorp has a revolving credit agreement with various banks for a \$500 million borrowing facility. Interest is at variable rates and the facility matures in February 2011. The amounts outstanding as of December 31, 2009 and 2008 were \$220 million and \$300 million, respectively, bearing average interest rates of 0.5% and 3.7%, respectively. As of and during the year ended December 31, 2009, Pacific LifeCorp was in compliance with the debt covenants related to this facility.

ACG has a revolving credit agreement with a bank for a \$105 million borrowing facility, which was entered into in May 2009. Interest is at variable rates and the facility matures in April 2010. The amount outstanding as of December 31, 2009 was \$105 million, bearing an interest rate of 4.8%. As of and during the year ended December 31, 2009, ACG was in compliance with the debt covenants related to this facility. This credit facility is recourse only to ACG.

ACG had a revolving credit agreement with a bank for a \$150 million borrowing facility, which was entered into in April 2008. The amount outstanding as of December 31, 2008 was \$150 million, bearing an interest rate of 2.3%. This credit facility matured and was repaid in May 2009.

PAF had a revolving credit agreement of \$50 million. Interest was at variable rates and the facility matured in October 2009. The amount outstanding as of December 31, 2008 under a different facility that matured in July 2009 was \$15 million, bearing an average interest rate of 2.2%.

Pacific Life maintains a \$700 million commercial paper program. There was no commercial paper debt outstanding as of December 31, 2009 and 2008. In addition, Pacific Life has a bank revolving credit facility of \$400 million maturing in 2012 that serves as a back-up line of credit for the commercial paper program. This facility had no debt outstanding as of December 31, 2009 and 2008. As of and during the year ended December 31, 2009, Pacific Life was in compliance with the debt covenants related to this facility.

PL&A maintains a \$40 million reverse repurchase line of credit with a commercial bank. These borrowings are at variable rates of interest based on collateral and market conditions. There was no debt outstanding in connection with this line of credit as of December 31, 2009 and 2008.

Pacific Life is a member of the FHLB of Topeka. Pacific Life has approval from the FHLB of Topeka to advance amounts up to 40% of Pacific Life's statutory general account assets provided it has available collateral and is in compliance with debt covenant restrictions and insurance laws and regulations. There was no debt outstanding with the FHLB of Topeka as of December 31, 2009 and 2008. The Company had \$127 million and \$1.0 billion of additional funding capacity from eligible collateral as of December 31, 2009 and 2008, respectively.

PL&A is a member of the FHLB of San Francisco. PL&A is eligible to borrow from the FHLB of San Francisco amounts based on a percentage of statutory capital and surplus and could borrow up to amounts of \$102 million. Of this amount, half, or \$51 million, can be borrowed for terms other than overnight, out to a maximum term of nine months. These borrowings are at variable rates of interest, collateralized by certain mortgage loan and government securities. As of December 31, 2009 and 2008, PL&A had no debt outstanding with the FHLB of San Francisco.

College Savings Bank (CSB), a wholly owned subsidiary, finances a portion of its investment securities by entering into repurchase agreements with financial institutions and U.S. government agencies. As of December 31, 2009 and 2008, the outstanding balance amounted to \$214 million and \$195 million, respectively, with weighted-average interest rates of 0.5% and 3.0%, respectively. The weighted-average remaining maturity of repurchase agreements as of December 31, 2009 was 33 days. CSB manages its daily liquidity by purchasing overnight Federal funds with financial institutions and/or borrowing from the Federal Discount Window. As of December 31, 2009, there were no additional borrowings. As of December 31, 2008, CSB borrowed \$75 million under a 14 day term loan, and \$64 million on an overnight basis from the Federal Discount Window, both carrying an interest rate of 0.5%.

LONG-TERM DEBT

In June 2009, Pacific Life issued \$1.0 billion of surplus notes at a fixed interest rate of 9.25%, maturing on June 15, 2039. Interest is payable semiannually on June 15 and December 15. Pacific Life may redeem the 9.25% surplus notes at its option, subject to the approval of the Nebraska Director of Insurance for such optional redemption. The 9.25% surplus notes are unsecured and subordinated to all present and future senior indebtedness and policy claims of Pacific Life. All future payments of interest and principal on the 9.25% surplus notes can be made only with the prior approval of the Nebraska Director of Insurance. The Company entered into interest rate swaps converting \$650 million of these surplus notes to variable rate notes based upon the London InterBank Offered Rate (LIBOR). The interest rate swaps were designated as fair value hedges of these surplus notes and the changes in fair value of the hedged surplus notes associated with changes in interest rates are reflected as an adjustment to their carrying amount. This adjustment to the carrying amount of the surplus notes, which decreased long-term debt by \$35 million as of December 31, 2009, is offset by a fair value adjustment which has also been recorded for the interest rate swap derivative instruments.

Pacific Life has \$150 million of surplus notes outstanding at a fixed interest rate of 7.9%, maturing on December 30, 2023. Interest is payable semiannually on June 30 and December 30. The 7.9% surplus notes may not be redeemed at the option of Pacific Life or any holder of the surplus notes. The 7.9% surplus notes are unsecured and subordinated to all present and future senior

indebtedness and policy claims of Pacific Life. All future payments of interest and principal on the 7.9% surplus notes can be made only with the prior approval of the Nebraska Director of Insurance. The Company entered into interest rate swaps converting these surplus notes to variable rate notes based upon the LIBOR. The interest rate swaps were designated as fair value hedges of these surplus notes and the changes in fair value of the hedged surplus notes associated with changes in interest rates are reflected as an adjustment to their carrying amount. This adjustment to the carrying amount of the surplus notes, which increased long-term debt by \$22 million and \$55 million as of December 31, 2009 and 2008, respectively, is offset by a fair value adjustment which has also been recorded for the interest rate swap derivative instruments.

Pacific LifeCorp has \$600 million of senior notes outstanding at a fixed interest rate of 6.6%, maturing on September 15, 2033. Interest is payable semiannually on March 15 and September 15. Pacific LifeCorp may redeem all or a portion of the senior notes at any time at the redemption price described under the terms of the senior notes. The Company entered into interest rate swaps converting these senior notes to variable rate notes based upon the LIBOR. The interest rate swaps were designated as fair value hedges of these senior notes. In 2008 and 2005, the interest rate swaps were terminated and gains of \$181 million and \$110 million, respectively, were deferred as an adjustment to the carrying amount of the senior notes. Total unamortized deferred gains are \$277 million and \$284 million as of December 31, 2009 and 2008, respectively.

ACG enters into various term loans with third-parties. Interest on these loans is payable monthly, quarterly or semi-annually and ranged from 0.3% to 6.8% as of December 31, 2009 and from 1.7% to 6.8% as of December 31, 2008. As of December 31, 2009, \$1,636 million was outstanding on these loans with maturities ranging from 2010 to 2021. Principal payments due over the next twelve months are \$297 million. As of December 31, 2008, \$1,271 million was outstanding on these loans. These loans are recourse only to ACG.

ACG enters into various acquisition facilities and bank loans to acquire aircraft. Interest on these facilities and loans accrues at variable rates, is payable monthly and ranged from 1.6% to 3.2% as of December 31, 2009 and from 2.0% to 3.0% as of December 31, 2008. As of December 31, 2009, \$761 million was outstanding on these facilities and loans with maturities ranging from 2010 to 2014. As of December 31, 2008, \$687 million was outstanding on these facilities and loans. These facilities and loans are non-recourse to the Company.

Certain subsidiaries of Pacific Asset Holding LLC (PAH), a wholly owned subsidiary of Pacific Life, entered into various term loans with third-parties. Interest on these loans accrues at fixed rates, is payable monthly and ranged from 5.8% to 6.2% as of December 31, 2009 and 2008. As of December 31, 2009 and 2008, there was \$87 million outstanding on these loans with maturities ranging from 2010 to 2012. Principal payments due over the next twelve months are \$32 million. All of these loans are secured by real estate properties and are non-recourse to the Company.

Certain subsidiaries of PAH also entered into various property improvement loans with third-parties for a maximum loan balance of \$43 million. Interest on these loans accrues at variable rates, is payable monthly and ranged from 1.4% and 2.0% as of December 31, 2009 and 2.6% to 3.6% as of December 31, 2008. As of December 31, 2009 and 2008, there was \$34 million outstanding on these loans with maturities ranging from 2010 to 2011. Principal payments due over the next twelve months are \$26 million. All of these loans are secured by real estate properties and are non-recourse to the Company.

15. FAIR VALUE OF FINANCIAL INSTRUMENTS

The Codification's Fair Value Measurements and Disclosures Topic establishes a hierarchy that prioritizes the inputs of valuation methods used to measure fair value for financial assets and financial liabilities that are carried at fair value. The hierarchy consists of the following three levels that are prioritized based on observable and unobservable inputs.

- | | |
|---------|--|
| Level 1 | Unadjusted quoted prices for identical instruments in active markets. Level 1 financial instruments would include securities that are traded in an active exchange market. |
| Level 2 | Observable inputs other than Level 1 prices, such as quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in inactive markets; and model-derived valuations for which all significant inputs are observable market data. Level 2 instruments include most corporate debt securities and U.S. government and agency mortgage-backed securities that are valued by models using inputs that are derived principally from or corroborated by observable market data. |
| Level 3 | Valuations derived from valuation techniques in which one or more significant inputs are unobservable. Level 3 instruments include less liquid securities for which significant inputs are not observable in the market, such as highly structured securities and variable annuity GLB embedded derivatives that require significant management assumptions or estimation in the fair value measurement. |

This hierarchy requires the use of observable market data when available.

The following tables present, by fair value hierarchy level, the Company's financial assets and liabilities that are carried at fair value as of December 31, 2009 and 2008.

	Level 1	Level 2	Level 3	Gross Derivatives Fair Value	Netting Adjustments ⁽¹⁾	Total
<i>(In Millions)</i>						
<u>December 31, 2009:</u>						
Assets:						
U.S. Treasury securities and obligations of						
U.S. government authorities and agencies		\$122	\$6			\$128
Obligations of states and political subdivisions		569	34			603
Foreign governments		324	108			432
Corporate securities		15,832	2,295			18,127
RMBS		1,753	3,752			5,505
CMBS		853	327			1,180
Collateralized debt obligations		8	104			112
Other asset-backed securities		360	235			595
Total fixed maturity securities		19,821	6,861			26,682
Perpetual preferred securities		237	70			307
Other equity securities	\$68					68
Total equity securities	68	237	70			375
Trading securities ⁽²⁾	92	85	29			206
Cash equivalents	1,725					1,725
Other investments			180			180
Derivatives		462	468	\$930	(\$694)	236
Separate account assets ⁽³⁾	52,305	116	101			52,522
Total	\$54,190	\$20,721	\$7,709	\$930	(\$694)	\$81,926
Liabilities:						
Derivatives		\$769	\$915	\$1,684	(\$694)	\$990
Total		\$769	\$915	\$1,684	(\$694)	\$990

	Level 1	Level 2	Level 3	Gross Derivatives Fair Value	Netting Adjustments ⁽¹⁾	Total
<i>(In Millions)</i>						
<u>December 31, 2008:</u>						
Assets:						
U.S. Treasury securities and obligations of						
U.S. government authorities and agencies		\$122				\$122
Obligations of states and political subdivisions		369				369
Foreign governments		324	\$22			346
Corporate securities		12,445	2,247			14,692
RMBS		1,946	3,356			5,302
CMBS		902	201			1,103
Collateralized debt obligations		20	104			124
Other asset-backed securities		336	210			546
Total fixed maturity securities		16,464	6,140			22,604
Perpetual preferred securities		202	15			217
Other equity securities		2				2
Total equity securities		204	15			219
Trading securities ⁽²⁾		17	97			114
Cash equivalents	\$2,653					2,653
Other investments			168			168
Derivatives		1,345	1,435	\$2,780	(\$678)	2,102
Separate account assets ⁽³⁾	41,145	275	61			41,481
Total	\$43,798	\$18,305	\$7,916	\$2,780	(\$678)	\$69,341
Liabilities:						
Derivatives		\$1,197	\$3,477	\$4,674	(\$678)	\$3,996
Total		\$1,197	\$3,477	\$4,674	(\$678)	\$3,996

⁽¹⁾ Netting adjustments represent the impact of offsetting asset and liability positions held with the same counterparty as permitted by guidance for offsetting in the Codification's Derivatives and Hedging Topic.

⁽²⁾ Trading securities are presented in other investments in the consolidated statements of financial condition.

⁽³⁾ Separate account assets are measured at fair value. Investment performance related to separate account assets is offset by corresponding amounts credited to contract holders whose liability is reflected in the separate account liabilities. Separate account liabilities are measured to equal the fair value of separate account assets as prescribed by guidance in the Codification's Financial Services – Insurance Topic for accounting and reporting of certain non traditional long-duration contracts and separate accounts. Separate account assets as presented in the table above differ from the amounts presented in the consolidated statements of financial condition because cash and receivables for securities are not subject to the guidance under the Codification's Fair Value Measurements and Disclosures Topic.

FAIR VALUE MEASUREMENT

The Codification's Fair Value Measurements and Disclosures Topic defines fair value as the price that would be received to sell the asset or paid to transfer the liability at the measurement date. This "exit price" notion is a market-based measurement that requires a focus on the value that market participants would assign for an asset or liability.

The following section describes the valuation methodologies used by the Company to measure various types of financial instruments at fair value.

FIXED MATURITY, EQUITY AND TRADING SECURITIES

The fair values of fixed maturity securities available for sale, equity securities available for sale and trading securities are determined by management after considering external pricing sources and internal valuation techniques.

For publicly traded securities with sufficient trading volume, prices are obtained from third-party pricing services. For structured or complex securities that are traded infrequently, prices are obtained from independent brokers or are valued internally using various valuation techniques. Such techniques include matrix model pricing and internally developed models, which incorporate observable market data, where available. Matrix model pricing measures fair value using cash flows, which are discounted using observable market yield curves provided by a major independent data service. The matrix model determines the discount yield based upon significant factors that include the security's weighted average life and rating.

Where matrix model pricing is not used, particularly for RMBS and other asset-backed securities, other internally derived valuation models are utilized. The inputs used to measure fair value in the internal valuations include, but are not limited to, benchmark yields, issuer spreads, bids, offers, reported trades, and estimated projected cash flows that incorporate significant inputs such as defaults and delinquency rates, severity, subordination, vintage and prepayment speeds.

For non-agency RMBS backed by prime, sub-prime and Alt-A collateral, the Company has determined that there has been a significant decrease in the volume and level of transaction activity indicating the need for a valuation technique not solely based on observable transactions and/or quoted market prices. As permitted by guidance in the Codification's Fair Value Measurements and Disclosures Topic beginning March 31, 2009, the Company determines the estimated fair value for these assets utilizing an internally developed weighting of valuations derived from internal pricing models and independent pricing services. This approach utilizes multiple valuation techniques incorporating an income approach (maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs) and a market approach (based on data provided by independent pricing services) producing a result more representative of an investment's fair value as compared to a single valuation technique. The income approach incorporates cash flows for each investment adjusted for expected losses assuming various interest rate and housing price-level scenarios. The adjusted cash flows are discounted using a risk premium that market participants would demand given the risk in the modeled cash flows. The risk premium utilized is reflective of an orderly transaction between market participants under current market conditions and includes considerations such as liquidity and structure risk. These internally generated prices are then reviewed in conjunction with prices obtained from multiple independent pricing services. The internally generated prices are weighted with the prices obtained from independent pricing services, with consideration given to the relative range of values that are most representative of fair value under current conditions. These securities have been classified as Level 3 financial assets.

Prices obtained from independent third-parties are generally evaluated based on the inputs indicated above. The Company's management analyzes and evaluates these prices and determines whether they are reasonable estimates of fair value. Management's analysis may include, but is not limited to, review of third-party pricing methodologies and inputs, analysis of recent trades, and development of internal models utilizing observable market data of comparable securities. Based on this analysis, prices received from third-parties may be adjusted if the Company determines that there is a more appropriate fair value based on available market information.

Most securities priced by a major independent third-party service have been classified as Level 2, as management has verified that the inputs used in determining their fair values are market observable and appropriate. Other externally priced securities for which fair value measurement inputs are not sufficiently transparent, such as securities valued based on broker quotations, have been classified as Level 3. Internally valued securities, including adjusted prices received from independent third-parties, where significant management assumptions have been utilized in determining fair value, have been classified as Level 3.

CASH EQUIVALENTS

Cash equivalents include, but are not limited to, corporate discount notes and money market mutual funds. The fair value of cash equivalents is measured at amortized cost due to the short-term, highly liquid nature of these securities, which have original maturities of three months or less. These investments are classified as Level 1.

OTHER INVESTMENTS

Other investments include non-marketable equity securities that do not have readily determinable fair values. Certain significant inputs used in determining the fair value of these equities are based on management assumptions or contractual terms with another party that cannot be readily observable in the market. These investments are classified as Level 3 assets.

DERIVATIVE INSTRUMENTS

Derivative instruments are reported at fair value using pricing valuation models, which utilize market data inputs or independent broker quotations. Excluding embedded derivatives, as of December 31, 2009, 99% of derivatives based upon notional values were priced by valuation models, which utilize independent market data. The remaining derivatives were priced by broker quotations. The derivatives are valued using mid-market inputs that are predominantly observable in the market. Inputs used to value derivatives include, but are not limited to, interest swap rates, foreign currency forward and spot rates, credit spreads and correlations, interest and equity volatility and equity index levels. In accordance with the Codification's Fair Value Measurements and Disclosures Topic, a credit valuation analysis was performed for all derivative positions to measure the risk that one of the counterparties to the transaction will be unable to perform under the contractual terms (nonperformance risk), and was determined to be immaterial as of December 31, 2009.

The Company performs a monthly analysis on derivative valuations, which includes both quantitative and qualitative analysis. Examples of procedures performed include, but are not limited to, review of pricing statistics and trends, analyzing the impacts of changes in the market environment, and review of changes in market value for each derivative including those derivatives priced by brokers.

Derivative instruments classified as Level 2 primarily include interest rate, currency and certain credit default swaps. The derivative valuations are determined using pricing models with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Derivative instruments classified as Level 3 include complex derivatives, such as equity options and swaps and certain credit default swaps. Also included in Level 3 classification for derivatives are embedded derivatives in certain insurance and reinsurance contracts. These derivatives are valued using pricing models, which utilize both observable and unobservable inputs and, to a lesser extent, broker quotations. A derivative instrument containing Level 1 or 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 instrument may not be classified within the same fair value hierarchy level as the associated assets and liabilities. Therefore, the realized and unrealized gains and losses on derivatives reported in Level 3 may not reflect the offsetting impact of the realized and unrealized gains and losses of the associated assets and liabilities.

VARIABLE ANNUITY GLB EMBEDDED DERIVATIVES

Fair values for variable annuity GLB and related reinsurance embedded derivatives are calculated based upon significant unobservable inputs using internally developed models because active, observable markets do not exist for those items. As a result, variable annuity GLB and related reinsurance embedded derivatives are categorized as Level 3. Below is a description of the Company's fair value methodologies for these embedded derivatives.

The Company's fair value is calculated as an aggregation of fair value and additional risk margins including, Behavior Risk Margin, Mortality Risk Margin and Credit Standing Adjustment. The resulting aggregation is reconciled or calibrated, if necessary, to market information that is, or may be, available to the Company, but may not be observable by other market participants, including reinsurance discussions and transactions. Each of the components described below are unobservable in the market place and requires subjectivity by the Company in determining their value.

- Behavior Risk Margin: This component adds a margin that market participants would require for the risk that the Company's assumptions about policyholder behavior used in the fair value model could differ from actual experience.
- Mortality Risk Margin: This component adds a margin in mortality assumptions, both for decrements for policyholders with GLBs, and for expected payout lifetimes in guaranteed minimum withdrawal benefits.
- Credit Standing Adjustment: This component makes an adjustment that market participants would make to reflect the chance that GLB obligations or the GLB reinsurance recoverables will not be fulfilled (nonperformance risk).

SEPARATE ACCOUNT ASSETS

Separate account assets are primarily invested in mutual funds, but also have investments in fixed maturity and short-term securities. Separate account assets are valued in the same manner, and using the same pricing sources and inputs, as the fixed maturity and equity securities available for sale of the Company. Mutual funds are included in Level 1. Most fixed maturity securities are included in Level 2. Level 3 assets include any investments where fair value is based on management assumptions or obtained from independent third-parties and fair value measurement inputs are not sufficiently transparent.

LEVEL 3 RECONCILIATION

The tables below present reconciliations of the beginning and ending balances of the Level 3 financial assets and liabilities that have been measured at fair value on a recurring basis using significant unobservable inputs.

	January 1, 2009	Total Gains or Losses		Transfers In and/or Out of Level 3	Purchases, Sales, Issuances, and Settlements	December 31, 2009	Unrealized Gains (Losses) Still Held ⁽¹⁾
		Included in Earnings	Included in OCI				
<i>(In Millions)</i>							
Assets:							
U.S. Treasury securities and obligations of U.S. government authorities and agencies				\$6		\$6	
Obligations of states and political subdivisions			(\$3)	7	\$30	34	
Foreign governments	\$22	\$2	5	71	8	108	
Corporate securities	2,247	(29)	646	(974)	405	2,295	(\$5)
RMBS	3,356	(115)	436	436	(361)	3,752	
CMBS	201	1	26	60	39	327	
Collateralized debt obligations	104	(67)	71	2	(6)	104	
Other asset-backed securities	210	2	10	42	(29)	235	
Total fixed maturity securities	6,140	(206)	1,191	(350)	86	6,861	(5)
Perpetual preferred securities	15	(17)	12	(8)	68	70	
Other equity securities		1	4	(28)	23		
Total equity securities	15	(16)	16	(36)	91	70	
Trading securities	97			(51)	(17)	29	2
Other investments	168		24		(12)	180	
Derivatives, net	(2,042)	1,504	1		90	(447)	1,597
Separate account assets ⁽²⁾	61	6		20	14	101	12
Total	\$4,439	\$1,288	\$1,232	(\$417)	\$252	\$6,794	\$1,606

	January 1, 2008	Total Gains or Losses		Transfers In and/or Out of Level 3	Purchases, Sales, Issuances, and Settlements	December 31, 2008	Unrealized Gains (Losses) Still Held ⁽¹⁾
		Included in Earnings	Included in OCI				
<i>(In Millions)</i>							
Assets:							
Foreign governments	\$32		(\$7)		(\$3)	\$22	
Corporate securities	1,505	\$2	(331)	\$733	338	2,247	(\$17)
RMBS	431	(1)	(168)	3,027	67	3,356	
CMBS	434		(40)	(141)	(52)	201	
Collateralized debt obligations	230	(90)	(35)		(1)	104	
Other asset-backed securities	242	(4)	(16)	(11)	(1)	210	
Total fixed maturity securities	<u>2,874</u>	<u>(93)</u>	<u>(597)</u>	<u>3,608</u>	<u>348</u>	<u>6,140</u>	<u>(17)</u>
Perpetual preferred securities	46	(33)	(1)	1	2	15	
Other equity securities	4	(4)					
Total equity securities	<u>50</u>	<u>(37)</u>	<u>(1)</u>	<u>1</u>	<u>2</u>	<u>15</u>	
Trading securities	47	(12)		10	52	97	(11)
Other investments	478	105	(133)		(282)	168	
Derivatives, net	(104)	(1,947)	2		7	(2,042)	(1,828)
Separate account assets ⁽²⁾	11	(5)		46	9	61	(25)
Total	<u>\$3,356</u>	<u>(\$1,989)</u>	<u>(\$729)</u>	<u>\$3,665</u>	<u>\$136</u>	<u>\$4,439</u>	<u>(\$1,881)</u>

⁽¹⁾ Represents the net amount of total gains or losses for the period, recorded in earnings, attributable to the change in unrealized gains (losses) relating to assets and liabilities classified as Level 3 that are still held as of December 31, 2009 and 2008.

⁽²⁾ The realized/unrealized gains (losses) included in net income (loss) for separate account assets are offset by an equal amount for separate account liabilities, which results in a net zero impact on net income (loss) for the Company.

The Company did not have any nonfinancial assets or liabilities measured at fair value on a nonrecurring basis resulting from impairments as of December 31, 2009. The Company has not made any changes in the valuation methodologies for nonfinancial assets and liabilities.

The carrying amount and estimated fair value of the Company's financial instruments that are not carried at fair value under the Codification's Financial Instruments Topic are as follows:

	<u>December 31, 2009</u>		<u>December 31, 2008</u>	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
	<i>(In Millions)</i>			
Assets:				
Mortgage loans	\$6,577	\$6,660	\$5,622	\$5,645
Policy loans	6,509	6,509	6,920	6,920
Other invested assets	196	185	322	351
Restricted cash	249	249	235	235
Other assets	323	323	407	407
Liabilities:				
Funding agreements and GICs ⁽¹⁾	7,572	8,093	9,419	10,136
Annuity and deposit liabilities	7,109	7,109	4,515	4,515
Short-term debt	539	539	799	799
Long-term debt	6,509	6,324	5,343	4,873
Other liabilities	341	341	251	251

⁽¹⁾ Balance excludes embedded derivatives that are included in the fair value hierarchy level tables above.

The following methods and assumptions were used to estimate the fair value of these financial instruments as of December 31, 2009 and 2008:

MORTGAGE LOANS

The estimated fair value of the mortgage loan portfolio is determined by discounting the estimated future cash flows, using current rates that are applicable to similar credit quality, property type and average maturity of the composite portfolio.

POLICY LOANS

The carrying amounts of policy loans are a reasonable estimate of their fair values because interest rates are generally variable and based on current market rates.

OTHER INVESTED ASSETS

Included in other invested assets are private equity investments in which the estimated fair value of private equity investments is based on the ownership percentage of the underlying equity of the investments.

RESTRICTED CASH

The carrying values approximate fair values due to the short-term maturities of these instruments.

OTHER ASSETS

Included in other assets are notes receivable and other loans in which the carrying amounts are a reasonable estimate of their fair value because interest rates are variable and based on current market rates.

FUNDING AGREEMENTS AND GICs

The fair value of funding agreements and GICs is estimated using the rates currently offered for deposits of similar remaining maturities.

ANNUITY AND DEPOSIT LIABILITIES

The estimated fair value of annuity and deposit liabilities approximates carrying value and primarily includes policyholder deposits and accumulated credited interest. The estimated fair value of deposit liabilities with no defined maturities is the amount payable on demand.

DEBT

The carrying amount of short-term debt is a reasonable estimate of its fair value because the interest rates are variable and based on current market rates. The estimated fair value of long-term debt is based on market quotes, except for VIE debt and non-recourse debt, for which the carrying amounts are reasonable estimates of their fair values because the interest rate approximates current market rates.

OTHER LIABILITIES

Other liabilities carrying amounts are a reasonable estimate of fair value because interest is variable and based on current market rates.

16. OTHER COMPREHENSIVE INCOME (LOSS)

The Company displays comprehensive income (loss) and its components on the consolidated statements of equity. The disclosure of the gross components of other comprehensive income (loss) and related taxes are as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Unrealized gain (loss) on derivatives and securities available for sale, net:			
Gross holding gain (loss):			
Securities available for sale	\$2,628	(\$3,875)	(\$232)
Derivatives	(141)	258	(149)
Income tax (expense) benefit	(879)	1,278	133
Reclassification adjustment - realized (gain) loss:			
Sale of securities available for sale	234	458	(21)
Derivatives	23	(2)	(13)
Income tax expense (benefit)	(92)	(160)	12
Allocation of holding (gain) loss to DAC	(413)	355	(24)
Allocation of holding (gain) loss to future policy benefits	85	(118)	(15)
Income tax expense (benefit)	113	(83)	14
Cumulative effect of adoption of new accounting principle	(263)		
Income tax expense	93		
Unrealized gain (loss) on derivatives and securities available for sale, net	<u>1,388</u>	<u>(1,889)</u>	<u>(295)</u>
Other, net:			
Holding gain (loss) on interest in PIMCO and other security	22	(24)	5
Income tax (expense) benefit	(8)	9	(1)
Reclassification of realized gain on sale of interest in PIMCO		(109)	
Income tax on realized gain		42	
Net unrealized gain (loss) on interest in PIMCO and other security	<u>14</u>	<u>(82)</u>	<u>4</u>
Cumulative effect of adoption of new accounting principle, net of tax			(20)
Other, net of tax	42	(56)	
Other, net	<u>56</u>	<u>(138)</u>	<u>(16)</u>
Total other comprehensive income (loss), net	<u>\$1,444</u>	<u>(\$2,027)</u>	<u>(\$311)</u>

17. REINSURANCE

Certain no lapse guarantee rider (NLGR) benefits of Pacific Life's UL insurance products are subject to Actuarial Guideline 38 (AG 38) statutory reserving requirements. AG 38 results in additional statutory reserves on UL products with NLGRs issued after June 30, 2005. U.S. GAAP benefit reserves for such riders are based on guidance in the Codification's Financial Services – Insurance Topic for accounting and reporting of certain non traditional long-duration contracts and separate accounts. Substantially all the U.S. GAAP benefit reserves relating to NLGRs issued after June 30, 2005 are ceded from Pacific Life to PAR Bermuda and PAR Vermont under reinsurance agreements. Funded reserves and irrevocable letters of credit (LOC) held in trust accounts with Pacific Life as beneficiary provide security for statutory reserve credits taken by Pacific Life. Pacific LifeCorp guarantees the obligations of PAR Bermuda and PAR Vermont under the LOC agreement.

The Company entered into treaties to reinsure a portion of new variable annuity business under modified coinsurance arrangements and certain variable annuity living and death benefit riders under coinsurance agreements. Effective January 1,

2008, the quota share on these variable annuity reinsurance treaties was increased from a total of 39% to 45%. Additionally, effective January 1, 2008, the Company recaptured a portion of the variable annuity business ceded during 2007. Effective January 1, 2009, all but one reinsurance treaty terminated for new business, reducing the quota share to 15%. The final treaty terminated for new business issued after March 31, 2009. Variable annuity business ceded prior to these dates continues to be reinsured.

Reinsurance receivables and payables generally include amounts related to claims, reserves and reserve related items. Reinsurance receivables were \$474 million and \$911 million as of December 31, 2009 and 2008, respectively. Reinsurance payables were \$49 million and \$52 million as of December 31, 2009 and 2008, respectively.

The ceding of risk does not discharge the Company from its primary obligations to contract owners. To the extent that the assuming companies become unable to meet their obligations under reinsurance contracts, the Company remains contingently liable. Each reinsurer is reviewed to evaluate its financial stability before entering into each reinsurance contract and throughout the period that the reinsurance contract is in place.

The components of insurance premiums presented in the consolidated statements of operations are as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Direct premiums	\$666	\$410	\$271
Reinsurance ceded	(308)	(280)	(262)
Reinsurance assumed	217	148	53
Insurance premiums	<u>\$575</u>	<u>\$278</u>	<u>\$62</u>

18. EMPLOYEE BENEFIT PLANS

PENSION PLANS

Prior to December 31, 2007, Pacific Life provided a defined benefit pension plan (ERP) covering all eligible employees of the Company. Certain subsidiaries did not participate in this plan. The full-benefit vesting period for all participants was five years. Pacific Life's funding policy was to contribute amounts to the plan sufficient to meet the minimum funding requirements set forth in ERISA, plus such additional amounts as was determined appropriate. All such contributions were made to a tax-exempt trust.

The Company amended the ERP to terminate effective December 31, 2007. In anticipation of the final settlement of the defined benefit pension plan, the plan's investment strategy was revised and the mutual fund investments were sold, transferred to a separate account group annuity contract managed by the Company and invested primarily in fixed income investments to better match the expected duration of the liabilities.

In September 2009, the Company received regulatory approval to commence the final termination of the ERP and payment of plan benefits to the participants. The Company completed the final distribution of plan assets to participants in December 2009. The Company recognized settlement costs of \$5 million in 2008 and recognized the final settlement costs for the ERP totaling \$72 million in 2009.

Pacific Life also maintains supplemental employee retirement plans (SERPs) for certain eligible employees. As of December 31, 2009 and 2008, the projected benefit obligation was \$37 million and \$32 million, respectively. The fair value of plan assets as of December 31, 2009 and 2008 was zero. The net periodic benefit expense of the SERPs was \$4 million, \$5 million and \$6 million for the years ended December 31, 2009, 2008 and 2007, respectively.

The following table sets forth the benefit obligations, plan assets and funded status of the defined benefit plans:

	December 31, 2009		December 31, 2008	
	ERP	SERP	ERP	SERP
	<i>(In Millions)</i>		<i>(In Millions)</i>	
<u>Defined benefit plans:</u>				
Benefit obligation, end of year		\$37	\$198	\$32
Fair value of plan assets, end of year	\$26		242	
Over (under) funded status, end of year	\$26	(\$37)	\$44	(\$32)

The Company incurred a net pension expense of \$79 million, \$8 million and \$9 million for the years ended December 31, 2009, 2008 and 2007, respectively, as detailed in the following table:

	Year Ended December 31, 2009		Year Ended December 31, 2008		Year Ended December 31, 2007	
	ERP	SERP	ERP	SERP	ERP	SERP
	<i>(In Millions)</i>		<i>(In Millions)</i>		<i>(In Millions)</i>	
<u>Components of the net periodic pension expense:</u>						
Service cost - benefits earned during the year		\$2		\$2		\$2
Interest cost on projected benefit obligation	\$12	2	\$12	2	\$14	2
Expected return on plan assets	(12)		(14)		(16)	
Settlement costs	72		5		4	
Amortization of net obligations and prior service cost	3			1	2	1
Net periodic pension expense	\$75	\$4	\$3	\$5	\$4	\$5

Significant plan assumptions:

	December 31, 2009		December 31, 2008	
	ERP	SERP	ERP	SERP
<u>Weighted-average assumptions used to determine benefit obligations:</u>				
Discount rate	6.35%	6.30%	6.35%	6.30%
Salary rate	N/A	4.50%	N/A	4.50%

	Years Ended December 31,		
	2009	2008	2007
<u>Weighted-average assumptions used to determine the ERP's net periodic benefit expense:</u>			
Discount rate	6.30%	6.25%	5.75%
Expected long-term return on plan assets	N/A	5.25%	6.13%

The salary rate used to determine the net periodic benefit expense for the SERP was 4.5% for the years ended December 31, 2009, 2008 and 2007.

Pacific Life expects to contribute \$3 million to the SERP in 2010. The expected benefit payments are as follows for the years ending December 31 *(In Millions)*:

2010	2011	2012	2013	2014	2015-2019
\$3	\$3	\$3	\$3	\$3	\$15

RETIREMENT INCENTIVE SAVINGS PLAN

Pacific Life provides a Retirement Incentive Savings Plan (RISP) covering all eligible employees of Pacific LifeCorp and certain of its subsidiaries. The RISP matches 75% of each employee's contributions, up to a maximum of 6% of eligible employee compensation in cash. Contributions made by the Company to the RISP amounted to \$26 million, \$29 million and \$25 million for the years ended December 31, 2009, 2008 and 2007, respectively, and are included in operating expenses.

POSTRETIREMENT BENEFITS

Pacific Life provides a defined benefit health care plan and a defined benefit life insurance plan (the Plans) that provide postretirement benefits for all eligible retirees and their dependents. Generally, qualified employees may become eligible for these benefits if they have reached normal retirement age, have been covered under Pacific Life's policy as an active employee for a minimum continuous period prior to the date retired, and have an employment date before January 1, 1990. The Plans contain cost-sharing features such as deductibles and coinsurance, and require retirees to make contributions, which can be adjusted annually. Pacific Life's commitment to qualified employees who retire after April 1, 1994 is limited to specific dollar amounts. Pacific Life reserves the right to modify or terminate the Plans at any time. As in the past, the general policy is to fund these benefits on a pay-as-you-go basis.

The net periodic postretirement benefit cost for each of the years ended December 31, 2009, 2008 and 2007 was \$1 million. As of December 31, 2009 and 2008, the accumulated benefit obligation was \$19 million and \$18 million, respectively. The fair value of the plan assets as of December 31, 2009 and 2008 was zero.

The discount rate used in determining the accumulated postretirement benefit obligation was 5.50% and 6.35% for 2009 and 2008, respectively.

Benefit payments for the year ended December 31, 2009 amounted to \$3 million. The expected benefit payments are as follows for the years ending December 31 (*In Millions*):

<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015-2019</u>
\$3	\$4	\$4	\$4	\$4	\$24

OTHER PLANS

The Company has deferred compensation plans that permit eligible employees to defer portions of their compensation and earn interest on the deferred amounts. The interest rate is determined annually. The compensation that has been deferred has been accrued and the primary expense related to this plan, other than compensation, is interest on the deferred amounts. The Company also has performance-based incentive compensation plans for its employees.

19. INCOME TAXES

The provision (benefit) for income taxes is as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Current	(\$417)	\$196	\$24
Deferred	441	(535)	88
Provision (benefit) for income taxes from continuing operations	24	(339)	112
Provision (benefit) for income taxes on discontinued operations	(11)	(3)	18
Total	\$13	(\$342)	\$130

A reconciliation of the provision (benefit) for income taxes from continuing operations based on the Federal corporate statutory tax rate of 35% to the provision (benefit) for income taxes from continuing operations reflected in the consolidated financial statements is as follows:

	Years Ended December 31,		
	2009	2008	2007
	<i>(In Millions)</i>		
Provision (benefit) for income taxes at the statutory rate	\$163	(\$219)	\$275
Separate account dividends received deduction	(93)	(107)	(103)
Low income housing and foreign tax credits	(19)	(31)	(33)
Other	(27)	18	(27)
Provision (benefit) for income taxes from continuing operations	<u>\$24</u>	<u>(\$339)</u>	<u>\$112</u>

Upon adoption of new guidance to the Codification's Income Taxes Topic relating to the accounting for uncertainty in income taxes on January 1, 2007, the Company had unrecognized tax benefits of \$32 million, which relate entirely to an uncertain tax position regarding refund claims for the impact of short-term capital gains on computing separate account Dividends Received Deductions (DRD).

During the year ended December 31, 2008, the Company's tax contingency related to the accounting for uncertainty in income taxes increased by \$402 million for a tax position for which there was uncertainty about the timing, but not the deductibility, of certain tax deductions. Since the benefits of the tax position were not being claimed on an original return and the Company did not receive cash, interest or penalties were not accrued. Due to the nature of deferred tax accounting, the tax position does not have an impact on the annual effective tax rate.

The \$434 million tax contingency related to the accounting for uncertainty in income taxes was decreased by \$420 million as a result of events that occurred during the year ended December 31, 2009. The Company effectively settled \$18 million of the gross uncertain tax position related to DRD, which resulted in the realization of \$9 million of tax benefits. The Company also resolved the uncertain tax accounting position on certain tax deductions resulting in a \$402 million decrease. The provision for income taxes from continuing operations has also been reduced by \$10 million for additional interest income resulting from favorable tax settlements.

A reconciliation of the changes in the unrecognized tax benefits is as follows *(In Millions)*:

Balance at January 1, 2007	\$32
Additions and deletions	
Balance at December 31, 2007	<u>32</u>
Additions and deletions	<u>402</u>
Balance at December 31, 2008	434
Additions and deletions	<u>(420)</u>
Balance at December 31, 2009	<u>\$14</u>

Depending on the outcome of Internal Revenue Service (IRS) audits, approximately \$7 million of the unrecognized DRD tax benefits may be realized during the next twelve months. All realized tax benefits and related interest are recorded as a discrete item that will impact the effective tax rate in the accounting period in which the uncertain tax position is ultimately settled.

During the years ended December 31, 2009, 2008 and 2007, the Company paid an immaterial amount of interest and penalties to state tax authorities.

The net deferred tax (liability) asset, included in other liabilities and other assets as of December 31, 2009 and 2008, respectively, is comprised of the following tax effected temporary differences:

	December 31,	
	2009	2008
	<i>(In Millions)</i>	
Deferred tax assets:		
Policyholder reserves	\$597	\$1,184
Tax net operating loss carryforward	426	290
Investment valuation	301	295
Tax credit carryforward	214	122
Deferred compensation	47	42
Maintenance reserves	38	46
Deferred revenue	15	15
Dividends to policyholders	8	8
Pacific Life Re valuation allowance	(14)	(19)
Other	2	5
Total deferred tax assets	<u>1,634</u>	<u>1,988</u>
Deferred tax liabilities:		
DAC	(1,319)	(1,225)
Depreciation	(563)	(458)
Reinsurance	(77)	(74)
Hedging	(42)	(14)
Partnership income	(27)	(65)
Retirement benefits		(19)
Other	(49)	(42)
Total deferred tax liabilities	<u>(2,077)</u>	<u>(1,897)</u>
Net deferred tax asset (liability) from continuing operations	(443)	91
Unrealized loss on derivatives and securities available for sale	101	959
Unrealized loss on interest in PIMCO and other security		8
Deferred taxes on cumulative changes in accounting principles	120	27
Minimum pension liability and other adjustments	(13)	5
Net deferred tax asset (liability)	<u>(\$235)</u>	<u>\$1,090</u>

The tax net operating loss carryforwards relate to Federal tax losses incurred in 1998 through 2008 with a 20-year carryforward for non-life losses and a 15-year carryforward for life losses, and California tax losses incurred in 2004 through 2008 with a ten-year carryforward.

The Codification's Income Taxes Topic requires separate footnote disclosure of the impact of foreign taxes. While the Company does have foreign operations, the results of those operations have not been separately disclosed since they are not material.

The Codification's Income Taxes Topic also requires the reduction of deferred tax assets by a valuation allowance if, based on the weight of available evidence, it is more likely than not that a portion or all of the deferred tax assets will not be realized. With the exception of a \$14 million and \$19 million valuation allowance that was recorded against deferred tax assets acquired with Pacific Life Re (Note 6) as of December 31, 2009 and 2008, respectively, based on management's assessment, it is more likely than not that the Company's deferred tax assets will be realized through future taxable income and the reversal of deferred tax liabilities.

The Company files income tax returns in U.S. Federal and various state jurisdictions. The Company is under continuous audit by the IRS and is audited periodically by some state taxing authorities. The IRS has completed audits of the Company's tax returns through the tax years ended December 31, 2005 and has commenced audits for tax years 2006, 2007 and 2008. The State of

California recently concluded audits for tax years 2003 and 2004 without a material assessment. The Company does not expect the Federal and state audits to result in any material assessments.

20. SEGMENT INFORMATION

The Company has four operating segments: Life Insurance, Investment Management, Annuities & Mutual Funds, and Aircraft Leasing. These segments are managed separately and have been identified based on differences in products and services offered. All other activity is included in the Corporate and Other segment.

The Life Insurance segment provides a broad range of life insurance products through multiple distribution channels operating in the upper income and corporate markets. Principal products include UL, VUL, survivor life, interest sensitive whole life, corporate-owned life insurance and traditional products such as whole life and term life. Distribution channels include regional life offices, marketing organizations, broker-dealer firms, wirehouses and M Financial, an association of independently owned and operated insurance and financial producers.

The Investment Management segment provides investment and insurance products to institutional investors, pension fund sponsors and structured settlement annuitants, primarily through its home office marketing team and other intermediaries. The segment's principal products include GICs, synthetic GICs, funding agreement-backed notes issued to institutional investors via medium-term note programs or to the FHLB of Topeka, as well as structured settlement annuities issued in conjunction with personal injury awards and group retirement annuities sold to pension plans.

The Annuities & Mutual Funds segment's principle products include variable and fixed annuities and mutual funds, and are offered through multiple distribution sources. Distribution channels include independent planners, financial institutions and national/regional wirehouses.

The Aircraft Leasing segment (Note 10) offers aircraft leasing to the airline industry throughout the world and provides brokerage and asset management services to other third-parties.

The Corporate and Other segment primarily includes investment income, expenses and assets not attributable to the operating segments, and the operations of certain subsidiaries that do not qualify as operating segments, primarily CSB, PAF and Pacific Life Re. The Corporate and Other segment also includes the interest in PIMCO and the elimination of intersegment transactions. Discontinued operations (Note 7) are also included in the Corporate and Other segment.

The Company uses the same accounting policies and procedures to measure segment net income (loss) and assets as it uses to measure its consolidated net income (loss) and assets. Net investment income and net realized investment gain (loss) are allocated based on invested assets purchased and held as is required for transacting the business of that segment. Overhead expenses are allocated based on services provided. Interest expense is allocated based on the short-term borrowing needs of the segment and is included in net investment income. The provision (benefit) for income taxes is allocated based on each segment's actual tax provision (benefit).

The operating segments, excluding Aircraft Leasing, are allocated equity based on formulas determined by management and receive a fixed interest rate of return on interdivision debentures supporting the allocated equity. The debenture amount is reflected as investment expense in net investment income in the Corporate and Other segment and as investment income in the operating segments.

The Company generates substantially all of its revenues and net income from customers located in the U.S. As of December 31, 2009 and 2008, the Company had foreign investments with an estimated fair value of \$7.4 billion and \$6.0 billion, respectively. Aircraft leased to foreign customers were \$5.0 billion and \$4.8 billion as of December 31, 2009 and 2008, respectively. Revenues derived from any customer did not exceed 10% of consolidated total revenues for the years ended December 31, 2009, 2008 and 2007.

The following is segment information as of and for the year ended December 31, 2009:

	Life	Investment	Annuities & Mutual	Aircraft	Corporate	Total
	Insurance	Management	Funds	Leasing	and Other	
REVENUES						
	<i>(In Millions)</i>					
Policy fees and insurance premiums	\$1,084	\$628	\$581		\$153	\$2,446
Net investment income	894	759	278	\$1	(35)	1,897
Net realized investment gain (loss)		55	313	7	(211)	164
OTTIs	(63)	(176)	(16)		(57)	(312)
Investment advisory fees	18		190			208
Aircraft leasing revenue				578		578
Inventory sales					80	80
Other income	11		112	13	14	150
Total revenues	1,944	1,266	1,458	599	(56)	5,211
BENEFITS AND EXPENSES						
Interest credited	681	379	193			1,253
Policy benefits	381	903	(40)		108	1,352
Commission expenses	353	18	320		14	705
Operating expenses	293	26	273	59	201	852
Cost of goods sold					80	80
Depreciation of aircraft				227		227
Interest expense				182	96	278
Total benefits and expenses	1,708	1,326	746	468	499	4,747
Income (loss) from continuing operations before provision (benefit) for income taxes	236	(60)	712	131	(555)	464
Provision (benefit) for income taxes	67	(24)	151	39	(209)	24
Income (loss) from continuing operations	169	(36)	561	92	(346)	440
Discontinued operations, net of taxes					(20)	(20)
Net income (loss)	169	(36)	561	92	(366)	420
Less: net (income) loss attributable to the noncontrolling interest from continuing operations				(9)	23	14
Net income (loss) attributable to the Company	\$169	(\$36)	\$561	\$83	(\$343)	\$434
Total assets	\$28,646	\$13,256	\$57,903	\$6,091	\$4,058	\$109,954
DAC	1,865	59	2,882		51	4,857
Separate account assets	5,590	67	46,907			52,564
Policyholder and contract liabilities	21,179	12,526	7,728		289	41,722
Separate account liabilities	5,590	67	46,907			52,564

The following is segment information as of and for the year ended December 31, 2008:

	Life Insurance	Investment Management	Annuities & Mutual Funds	Aircraft Leasing	Corporate and Other	Total
REVENUES						
	<i>(In Millions)</i>					
Policy fees and insurance premiums	\$956	\$363	\$691		\$93	\$2,103
Net investment income	855	876	178		120	2,029
Net realized investment gain (loss)	24	51	(768)		(74)	(767)
OTTIs	(69)	(398)	(30)	(\$3)	(84)	(584)
Realized investment gain on interest in PIMCO					109	109
Investment advisory fees	22		233			255
Aircraft leasing revenue				571		571
Inventory sales					98	98
Other income	12		117	38	29	196
Total revenues	1,800	892	421	606	291	4,010
BENEFITS AND EXPENSES						
Interest credited	661	440	133			1,234
Policy benefits	387	684	150		81	1,302
Commission expenses	268	18	429		8	723
Operating expenses	264	34	317	40	123	778
Cost of goods sold					95	95
Depreciation of aircraft				208		208
Interest expense				221	74	295
Total benefits and expenses	1,580	1,176	1,029	469	381	4,635
Income (loss) from continuing operations before provision (benefit) for income taxes	220	(284)	(608)	137	(90)	(625)
Provision (benefit) for income taxes	60	(103)	(329)	48	(15)	(339)
Income (loss) from continuing operations	160	(181)	(279)	89	(75)	(286)
Discontinued operations, net of taxes					(6)	(6)
Net income (loss)	160	(181)	(279)	89	(81)	(292)
Less: net (income) loss attributable to the noncontrolling interest from continuing operations				(8)	11	3
Net income (loss) attributable to the Company	\$160	(\$181)	(\$279)	\$81	(\$70)	(\$289)
Total assets	\$26,729	\$15,155	\$45,285	\$5,400	\$4,414	\$96,983
DAC	2,118	64	2,830		16	5,028
Separate account assets	4,525	284	36,696			41,505
Policyholder and contract liabilities	20,816	14,099	7,626		236	42,777
Separate account liabilities	4,525	284	36,696			41,505

The following is segment information for the year ended December 31, 2007:

	Life Insurance	Investment Management	Annuities & Mutual Funds	Aircraft Leasing	Corporate and Other	Total
<i>(In Millions)</i>						
REVENUES						
Policy fees and insurance premiums	\$789	\$224	\$779			\$1,792
Net investment income	803	905	186	\$9	\$254	2,157
Net realized investment gain (loss)	4	115	(99)	17	33	70
OTTIs	(3)	(95)				(98)
Investment advisory fees	29		298			327
Aircraft leasing revenue				535		535
Inventory sales					96	96
Other income	9		84	50	27	170
Total revenues	1,631	1,149	1,248	611	410	5,049
BENEFITS AND EXPENSES						
Interest credited	618	504	144			1,266
Policy benefits	315	535	12			862
Commission expenses	209	11	470			690
Operating expenses	252	34	346	49	126	807
Cost of goods sold					94	94
Depreciation of aircraft				189		189
Interest expense				261	94	355
Total benefits and expenses	1,394	1,084	972	499	314	4,263
Income from continuing operations before provision (benefit) for income taxes	237	65	276	112	96	786
Provision (benefit) for income taxes	60	12	(6)	32	14	112
Income from continuing operations	177	53	282	80	82	674
Discontinued operations, net of taxes					11	11
Net income	177	53	282	80	93	685
Less: net income attributable to the noncontrolling interest from continuing operations				(2)	(36)	(38)
Net income attributable to the Company	\$177	\$53	\$282	\$78	\$57	\$647

21. TRANSACTIONS WITH AFFILIATES

PLFA serves as the investment adviser for the Pacific Select Fund, an investment vehicle provided to the Company's variable life insurance policyholders and variable annuity contract owners, and the Pacific Life Funds, the investment vehicle for the Company's mutual fund products. Prior to May 1, 2007, Pacific Life served in this capacity. Investment advisory and other fees are based primarily upon the net asset value of the underlying portfolios. These fees, included in investment advisory fees and other income, amounted to \$244 million, \$287 million and \$337 million for the years ended December 31, 2009, 2008 and 2007, respectively. In addition, Pacific Life provides certain support services to the Pacific Select Fund and the Pacific Life Funds based on an allocation of actual costs. These fees amounted to \$4 million, \$3 million and \$3 million for the years ended December 31, 2009, 2008 and 2007, respectively.

In addition, effective May 1, 2007, a service plan adopted by the Pacific Select Fund went into effect whereby the fund pays PSD, as distributor of the fund, a service fee in connection with services rendered or procured to or for shareholders of the fund or their variable contract owners. These services may include, but are not limited to, payment of compensation to broker-dealers, including PSD itself, and other financial institutions and organizations, which assist in providing any of the services. For the years ended December 31, 2009 and 2008, PSD received \$86 million and \$100 million, respectively, in service fees from the Pacific Select Fund, which are recorded in other income. For the period May 1, 2007 through December 31, 2007, PSD received \$74 million in service fees from the Pacific Select Fund, which are also recorded in other income. The service fees were allocated to the operating segments, primarily the Annuities & Mutual Funds segment (Note 20).

22. COMMITMENTS AND CONTINGENCIES

COMMITMENTS

The Company has outstanding commitments to make investments primarily in mortgage loans, limited partnerships and other investments, as follows (*In Millions*):

<u>Years Ending December 31:</u>	
2010	\$1,005
2011 through 2014	494
2015 and thereafter	91
Total	<u>\$1,590</u>

The Company leases office facilities under various operating leases, which in most, but not all cases, are noncancelable. Rent expense, which is included in operating and other expenses, in connection with these leases was \$10 million, \$12 million and \$13 million for the years ended December 31, 2009, 2008 and 2007, respectively. In connection with the sale of a block of business in 2005, PL&A is contingently liable until March 31, 2013 for certain future rent and expense obligations, not to exceed \$15 million, related to an office lease that has been assigned to the buyer. Aggregate minimum future commitments are as follows (*In Millions*):

<u>Years Ending December 31:</u>	
2010	\$11
2011 through 2014	30
2015 and thereafter	4
Total	<u>\$45</u>

As of December 31, 2009, ACG has commitments with major aircraft manufacturers to purchase aircraft at an estimated delivery price of \$6,370 million with delivery from 2010 through 2017. Such purchase commitments may be funded:

- up to \$635 million in less than one year,
- an additional \$2,325 million in one to three years,
- an additional \$2,116 million in three to five years, and
- an additional \$1,021 million thereafter.

As of December 31, 2009, deposits related to these agreements totaled \$273 million and are included in other assets.

In connection with an acquisition in 2005, ACG assumed residual value support agreements with expiration dates ranging from 2011 to 2015. The gross remaining residual value exposure under these agreements was \$99 million as of December 31, 2009 and 2008. As of December 31, 2009, the Company has estimated that it has no measurable liability under the remaining residual value guarantee agreements.

As of December 31, 2009, PAF had credit limits available to various clients amounting to \$417 million. These companies had utilized approximately \$173 million of these credit limits as of December 31, 2009, of which \$163 million was funded in the form of notes receivable, inventory and trade receivables and \$10 million in the form of letters of credit and other commitments.

In connection with the reinsurance of NLGR benefits from Pacific Life to PAR Bermuda and PAR Vermont (Note 17), PAR Bermuda and PAR Vermont entered into a three year letter of credit agreement with a group of banks in April 2009. This agreement allows

for the issuance of letters of credit with an expiration date of March 2012 to PAR Bermuda and PAR Vermont for up to a combined total amount of \$650 million. As of December 31, 2009, a \$340 million letter of credit had been issued from this facility for PAR Bermuda. In addition, a letter of credit issued for PAR Vermont totaled \$52 million as of December 31, 2009. Pacific LifeCorp guarantees the obligations of PAR Bermuda and PAR Vermont under the letter of credit agreement.

In connection with the acquisition of Pacific Life Re (Note 6), Pacific LifeCorp provided a guarantee for the performance of certain obligations of Pacific Life Re. In addition, Pacific LifeCorp provided indemnification for certain matters, as set forth in the purchase agreement. As stated in the guarantee agreement, if Pacific Life Re is unable to meet its current obligations under unaffiliated reinsurance agreements, Pacific LifeCorp shall guarantee payment on any past, present and future obligations of Pacific Life Re. Management believes that any additional obligations, if any, related to this guarantee agreement is not likely to have a material adverse effect on the Company's consolidated financial statements.

CONTINGENCIES - LITIGATION

During the year ended December 31, 2007, Pacific Life settled a national class action lawsuit, *Cooper v. Pacific Life*, for a combination of cash distributions and contract credits to owners of qualified annuity contracts who purchased their contracts between August 19, 1998, and April 30, 2002, or paid premium payments during that time period. Pacific Life strongly disagreed with the claims in the lawsuit. The settlement is not considered an admission or concession with respect to any claims made in the lawsuit and did not have a material adverse effect on the Company's consolidated financial position. Initial distributions were made to eligible class members in the first quarter of 2008 with subsequent annual distributions for four years thereafter.

The Company is a respondent in a number of other legal proceedings, some of which involve allegations for extra-contractual damages. Although the Company is confident of its position in these matters, success is not a certainty and it is possible that in any case a judge or jury could rule against the Company. In the opinion of management, the outcome of such proceedings is not likely to have a material adverse effect on the Company's consolidated financial position. The Company believes adequate provision has been made in its consolidated financial statements for all probable and estimable losses for litigation claims against the Company.

CONTINGENCIES - IRS REVENUE RULING

On August 16, 2007, the IRS issued Revenue Ruling 2007-54, which provided the IRS' interpretation of tax law regarding the computation of the DRD. On September 25, 2007, the IRS issued Revenue Ruling 2007-61, which suspended Revenue Ruling 2007-54 and indicated the IRS would address the proper interpretation of tax law in a regulation project that is on the IRS' priority guidance plan. Although no guidance has been issued, if the IRS ultimately adopts the interpretation contained in Revenue Ruling 2007-54, the Company could lose a substantial amount of DRD tax benefits, which could have a material adverse effect on the Company's consolidated financial statements.

CONTINGENCIES - OTHER

In connection with the sale of certain broker-dealer subsidiaries (Note 7), certain indemnifications triggered by breaches of representations, warranties or covenants were provided by the Company. Also, included in the indemnifications is indemnification for certain third-party claims arising from the normal operation of these broker-dealers prior to the closing and within the nine month period following the sale. The Company believes adequate provision has been made in its consolidated financial statements for all probable and estimable losses for litigation claims against the Company.

In the course of its business, the Company provides certain indemnifications related to other dispositions, acquisitions, investments, lease agreements or other transactions that are triggered by, among other things, breaches of representations, warranties or covenants provided by the Company. These obligations are typically subject to time limitations that vary in duration, including contractual limitations and those that arise by operation of law, such as applicable statutes of limitation. Because the amounts of these types of indemnifications often are not explicitly stated, the overall maximum amount of the obligation under such indemnifications cannot be reasonably estimated. The Company has not historically made material payments for these types of indemnifications. The estimated maximum potential amount of future payments under these obligations is not determinable due to the lack of a stated maximum liability for certain matters, and therefore, no related liability has been recorded. Management believes that judgments, if any, against the Company related to such matters are not likely to have a material adverse effect on the Company's consolidated financial statements.

Most of the jurisdictions in which the Company is admitted to transact business require life insurance companies to participate in guaranty associations, which are organized to pay contractual benefits owed pursuant to insurance policies issued by insolvent life insurance companies. These associations levy assessments, up to prescribed limits, on all member companies in a particular state

based on the proportionate share of premiums written by member companies in the lines of business in which the insolvent insurer operated. The Company has not received notification of any insolvency that is expected to result in a material guaranty fund assessment.

In relation to the ACG Trust II securitization (Note 4), the Company is contingently obligated to purchase certain notes from ACG Trust II to cover shortfalls in amounts due to the holders of the notes, up to certain levels as specified under the related agreements. As of December 31, 2009, the maximum potential amount of this future investment commitment was \$100 million.

The Asset Purchase Agreements of Aviation Trust, ACG Trust II and ACG Trust III (Note 4) provide that Pacific LifeCorp will guarantee the performance of certain obligations of ACG, as well as provide certain indemnifications, and that Pacific Life will assume certain obligations of ACG arising from the breach of certain representations and warranties under the Asset Purchase Agreements. Management believes that obligations, if any, related to these guarantees are not likely to have a material adverse effect on the Company's consolidated financial statements. The financial debt obligations of Aviation Trust, ACG Trust II and ACG Trust III are non-recourse to the Company and are not guaranteed by the Company.

In connection with the operations of certain subsidiaries, the Company has made commitments to provide for additional capital funding as may be required.

See Note 11 for discussion of contingencies related to derivative instruments.

See Note 19 for discussion of other contingencies related to income taxes.

23. SUBSEQUENT EVENTS

The Company has evaluated events subsequent to December 31, 2009 and through March 4, 2010, the date the consolidated financial statements were available to be issued. The Company has not evaluated subsequent events after that date for presentation in these consolidated financial statements.

In February 2010, Pacific LifeCorp issued \$450 million of senior notes at a fixed interest rate of 6.0%, maturing on February 10, 2020. Interest is payable semiannually on February 10 and August 10. Pacific LifeCorp may redeem all or a portion of the notes at any time at the redemption price described under the terms of the senior notes.

As of January 1, 2010, the Board of Directors of Pacific LifeCorp and Pacific Life authorized a cash capital contribution to ACG in the amount of \$350 million, which could be made up to March 31, 2010.

Effective January 1, 2010, the Investment Management segment's products were moved into other segments of the Company. Structured settlement and group retirement annuities were moved to the Annuities & Mutual Fund segment and the other institutional investment products became part of the Corporate and Other segment.
