

*Pacific Mutual*  
*2010 Report to Members*





## PACIFIC MUTUAL

### *Contents*

- 1 *2010 Financial Summary*
- 2 *To Our Members*
- 6 *Condensed Consolidated Financial Statements*
- 11 *Notes to Condensed Consolidated Financial Statements*
- 36 *Independent Auditors' Report*
- 38 *Statement of Management's Responsibility*
- 39 *Directors*
- 40 *Senior Management*
- 41 *Contact Information*
- 41 *Annual Meeting Notice*

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The unabridged audited consolidated financial statements are available at [www.PacificLife.com/financials](http://www.PacificLife.com/financials). If a paper version is desired, please send a request via email to [PublicAffairs@PacificLife.com](mailto:PublicAffairs@PacificLife.com) or call (800) 800-7646, ext. 5002.

Pacific Life Insurance Company, a subsidiary of Pacific Mutual Holding Company, is licensed in all states except New York. In New York, individual life insurance and annuity products are available through Pacific Life & Annuity Company, a subsidiary of Pacific Life Insurance Company.

Product availability and features vary by state. Insurance product and rider guarantees are backed by the financial strength and claims-paying ability of the issuing company and do not protect the value of the variable investment options. Each company is solely responsible for the financial obligations accruing under the policies it issues.

Variable products are issued by Pacific Life Insurance Company and Pacific Life & Annuity Company. These products and mutual funds are distributed by **Pacific Select Distributors, Inc.** (member FINRA & SIPC), a subsidiary of Pacific Life Insurance Company and an affiliate of Pacific Life & Annuity Company, and are available through licensed third-party broker-dealers.

**PACIFIC MUTUAL HOLDING COMPANY** Pacific Mutual Holding Company (Pacific Mutual) is the parent company of Pacific LifeCorp, which is the parent company of Pacific Life Insurance Company. Policyholders and contract holders of Pacific Life Insurance Company are members of Pacific Mutual and, as such, are able to attend an annual meeting of Pacific Mutual and to elect its board of directors. Through its direct and indirect subsidiaries, Pacific Mutual is engaged in a wide variety of insurance, financial services, and other investment-related businesses.



## PACIFIC LIFE

**PACIFIC LIFE INSURANCE COMPANY** Offering insurance since 1868, Pacific Life<sup>1</sup> provides a wide range of life insurance products, annuities, and mutual funds, and offers a variety of investment products and services to individuals, businesses, and pension plans. Pacific Life also counts more than half of the 100 largest U.S. companies as its clients.<sup>2</sup>



## PACIFIC LIFE & ANNUITY COMPANY

**PACIFIC LIFE & ANNUITY COMPANY** Pacific Life & Annuity Company offers a wide range of products, including life insurance, annuities, structured settlement annuities, and other investment products and services for individuals and businesses.

<sup>1</sup> "Pacific Life" refers to Pacific Life Insurance Company and its affiliates, including Pacific Life & Annuity Company.

<sup>2</sup> Client count as of April 2010 is compiled by Pacific Life using the 2010 FORTUNE 500® list.



## Pacific Mutual Holding Company 2010 Financial Summary

Dollars In Millions	DECEMBER 31,	2010	2009	% Change
Company Assets		\$ 115,992	\$ 109,954	5%
Policyholder & Other Liabilities		\$ 108,448	\$ 103,575	5%
Equity <sup>1</sup>		\$ 7,017	\$ 6,537	7%
Operating Revenues <sup>2</sup>		\$ 5,800	\$ 5,359	8%
Operating Income <sup>3</sup>		\$ 587	\$ 520	13%
Deposits <sup>4</sup>		\$ 6,896	\$ 10,687	(35%)

### Company Assets IN BILLIONS OF DOLLARS



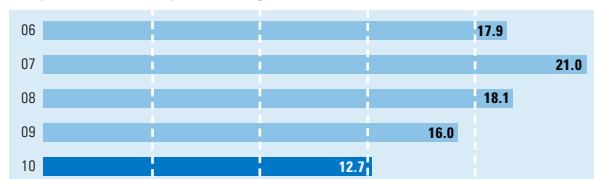
### Equity IN BILLIONS OF DOLLARS



### Operating Income IN MILLIONS OF DOLLARS



### Deposits & Operating Revenues IN BILLIONS OF DOLLARS



1 Excludes accumulated other comprehensive income/loss and noncontrolling interest.

2 Excludes net realized investment gains/losses and other than temporary impairments.

3 Excludes net realized investment gains/losses, other than temporary impairments, and discontinued operations, net of taxes.

4 Includes receipts from the following liabilities: universal life contracts, fixed and variable annuities, funding agreements, guaranteed interest contracts, and other deposits.

# To Our Members

While many financial institutions have faltered in recent years, Pacific Life remains an industry leader anchored by its strength and stability. Our competitive advantages range from our diverse array of products to our services that respond to the individual needs of our clients. These advantages are all created and produced by our dedicated employees. We call it *The Pacific Life Experience*: our promise to make every encounter with us an exceptional one.

We fulfill this promise by focusing on how to best accomplish the goals of our customers. We conduct business with the highest standards of integrity, and as a mutual company with no publicly traded stock, we make decisions based on what is best for our policyholders, unhindered by a need to maximize returns for shareholders.

As you know, a promise is only as good as the people who stand behind it. This is why, at Pacific Life, we choose to do business through the industry's most professional sales organizations and why we focus on attracting and retaining top talent. Our employees are passionate about our business and believe in what we do. This translates into the exceptional service that has helped us deliver security and peace of mind to millions of customers for 143 years.

**2010 FINANCIAL REVIEW** The year 2010 was a very successful one for our company. Given the current economic climate and the desire of customers to focus on financial security, we broadened the array of life insurance, annuity, and mutual fund products we offer, while maintaining our conservative investment and financial profile. Our focus on doing a few things very well produced solid results once again.

In 2010, our net income improved to \$480 million, an 11 percent increase over the prior year. All areas of the company, including the insurance and annuity businesses, the investment management and real estate areas, and our subsidiaries, contributed significantly to these results. Company assets grew to \$116 billion as we continued to provide value to existing and new clients. Company equity, the value of the company based on generally accepted accounting principles, reached the \$7 billion mark, the highest level in the company's history. Additionally, the regulatory capital level in our flagship, Pacific Life Insurance Company, grew 19 percent to its highest level ever at \$6.1 billion.

Our Life Insurance Division had a very strong operating year in spite of a volatile economic and sales environment. We are proud to be one of the top four<sup>1</sup> companies in the industry in sales by independent advisors of current assumption universal life, indexed universal life, and variable universal life products, each of which provides a combination of protection, certainty, and performance.

<sup>1</sup> LIMRA International, 2010 Confidential Sales Survey of Participating Life Insurance Companies. Sales rankings for Pacific Life Insurance Company are based on planned recurring premium as measured against 83 participating companies. Percentage increases are based on recurring premium vs. 2009 year-end results.

Our Retirement Solutions Division produced a solid bottom line and continued remarkable progress toward broadening its array of retirement offerings. While just two years ago, sales through this division were highly concentrated in the variable annuity product line, we now also achieve significant sales in fixed annuities. We had our best year ever in sales of mutual funds, where assets under management exceeded \$2 billion.

The results of the Life Insurance Division and the Retirement Solutions Division were considerably improved by the attractive yields and net returns delivered by our investment management professionals. We achieved significant gains in the diversified portfolio of assets managed within our Investment Management area. And for the fifth consecutive year, our mortgage loan portfolio, which is managed by the Real Estate Division, had no losses—a remarkable record in any environment, but especially during these turbulent economic conditions.

We're proud that our subsidiaries also achieved excellent results. Aviation Capital Group and Pacific Life Re both have customer bases that are almost entirely global, providing our company with participation in the growth that exists in international markets. These companies help make us a stronger financial company by providing attractive earnings and diversification.

Aviation Capital Group is one of the premier aircraft lessors in the world and has consistently produced bottom line increases year after year. Its earnings in 2010 were an impressive 40 percent increase over 2009.

Pacific Life Re, an international reinsurance company, once again delivered results that exceeded its very successful prior year by more than 17 percent. We are proud of the innovative and customized life reinsurance solutions that Pacific Life Re provides to its clients.

**ACKNOWLEDGEMENTS** A longtime member of the board of directors, Jim Ukropina, retired in 2010 following 21 years of service, the last four as lead director. Jim is currently the chief executive officer of Directions, LLC, after a career that included roles as chairman and

## 2010 Highlights

- Total consolidated assets of Pacific Mutual Holding Company reached \$116 billion, up 5 percent from 2009.
- Equity of Pacific Mutual Holding Company reached \$7.0 billion, compared with \$6.5 billion from the previous year.
- Life Insurance Division sales were \$232 million, compared with \$282 million in 2009.
- Retirement Solutions Division sales were \$5.4 billion, compared with \$8.0 billion in 2009.
- Revenues in Aviation Capital Group were \$648 million, compared with \$592 million in 2009.
- Generated earned premium income of \$232 million in our Pacific Life Re subsidiary.

chief executive officer of a public company and as a partner at a prestigious law firm. During his tenure on our board, he provided valuable insights through some remarkable periods of change and growth. We thank him for his wisdom and dedication.

Jacqueline Morby also retired from the board of directors in 2010 after 14 years of service. Jacqui is now a senior advisor of TA Associates after semiretiring from her 25-year career at the private equity firm. Her extensive business expertise, calm presence, and sound judgment helped make us a better company. We thank her for her guidance and contributions.

Julia Gouw was elected to the boards of Pacific Mutual Holding Company and Pacific LifeCorp in early 2011. As the president and chief operating officer of East West Bank, Julia brings a breadth of knowledge and experience to our boards. We look forward to her input on important business matters.

In late 2010, Mark Holmlund, executive vice president, Investment Management, left the company. Mark made significant contributions during his 17 years with us. He took an interest in people and was instrumental in the development of many Pacific Life employees. We are grateful to Mark and thank him for his years of service.

Audrey Milfs, vice president, retired after 38 years with the company, the last 27 serving as corporate secretary. Audrey was a very dedicated employee and demonstrated the highest of standards in all of her work. We thank her for her exemplary service to our company and our boards.

**LOOKING FORWARD** Financial security and certainty remain of paramount importance to clients today. At the same time, people are seeking to participate in the growth potential provided by improving economic conditions. Our products and services provide an array of choices for individuals and businesses and are well-positioned to accomplish these often conflicting goals. We thank you for your confidence in Pacific Life. Our goal is to make the experience you have with us a rewarding one.

**James T. Morris**

Chairman, President and Chief Executive Officer

# Financial Statements



Pacific Mutual Holding Company and Subsidiaries

# Condensed Consolidated Statements of Financial Condition

(In Millions) DECEMBER 31,

2010

2009

## ASSETS

### Investments:

Fixed maturity securities available for sale, at estimated fair value	<b>\$ 28,911</b>	\$ 26,682
Equity securities available for sale, at estimated fair value	<b>355</b>	375
Mortgage loans	<b>6,693</b>	6,577
Policy loans	<b>6,690</b>	6,509
Other investments (includes VIE assets of \$263 and \$232, respectively)	<b>2,284</b>	2,057

<b>TOTAL INVESTMENTS</b>	<b>44,933</b>	42,200
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Cash and cash equivalents (includes VIE assets of \$4 and \$7, respectively)	<b>2,433</b>	2,060
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Restricted cash (includes VIE assets of \$170 and \$190, respectively)	<b>226</b>	249
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Deferred policy acquisition costs	<b>4,560</b>	4,857
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Aircraft leasing portfolio, net (includes VIE assets of \$2,154 and \$2,384, respectively)	<b>5,259</b>	5,304
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Other assets (includes VIE assets of \$40 and \$48, respectively)	<b>2,898</b>	2,720
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Separate account assets	<b>55,683</b>	52,564
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<b>TOTAL ASSETS</b>	<b>\$ 115,992</b>	\$ 109,954
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## LIABILITIES AND EQUITY

### Liabilities:

Policyholder account balances	<b>\$ 35,076</b>	\$ 33,984
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Future policy benefits	<b>7,441</b>	7,738
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Short-term debt	<b>135</b>	539
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Long-term debt (includes VIE debt of \$1,592 and \$1,977, respectively)	<b>7,383</b>	6,509
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Other liabilities (includes VIE liabilities of \$385 and \$408, respectively)	<b>2,730</b>	2,241
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Separate account liabilities	<b>55,683</b>	52,564
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<b>TOTAL LIABILITIES</b>	<b>108,448</b>	103,575
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Commitments and contingencies (Note 10)

### Members' Equity:

Members' capital	<b>7,017</b>	6,537
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Accumulated other comprehensive income (loss)	<b>276</b>	(389)
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<b>Total Members' Equity</b>	<b>7,293</b>	6,148
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Noncontrolling interest	<b>251</b>	231
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<b>TOTAL EQUITY</b>	<b>7,544</b>	6,379
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<b>TOTAL LIABILITIES AND EQUITY</b>	<b>\$ 115,992</b>	\$ 109,954
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The abbreviation VIE above means variable interest entity.

See Notes to Condensed Consolidated Financial Statements

*Pacific Mutual Holding Company and Subsidiaries*  
**Condensed Consolidated Statements of Operations**

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
<b>REVENUES</b>			
Policy fees and insurance premiums	<b>\$ 2,550</b>	\$ 2,446	\$ 2,103
Net investment income	<b>2,156</b>	1,897	2,029
Net realized investment gain (loss)	<b>(84)</b>	164	(767)
OTTIs, consisting of \$328 and \$642 in total, net of \$215 and \$330 recognized in OCI for 2010 and 2009, respectively	<b>(113)</b>	(312)	(584)
Realized investment gain on interest in PIMCO			109
Investment advisory fees	<b>245</b>	208	255
Aircraft leasing revenue	<b>591</b>	578	571
Other income	<b>258</b>	230	294
<b>TOTAL REVENUES</b>	<b>5,603</b>	5,211	4,010
<b>BENEFITS AND EXPENSES</b>			
Policy benefits paid or provided	<b>1,468</b>	1,352	1,302
Interest credited to policyholder account balances	<b>1,317</b>	1,253	1,234
Commission expenses	<b>859</b>	705	723
Operating and other expenses	<b>1,379</b>	1,437	1,376
<b>TOTAL BENEFITS AND EXPENSES</b>	<b>5,023</b>	4,747	4,635
<b>INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE PROVISION (BENEFIT) FOR INCOME TAXES</b>			
	<b>580</b>	464	(625)
Provision (benefit) for income taxes	<b>50</b>	24	(339)
<b>INCOME (LOSS) FROM CONTINUING OPERATIONS</b>	<b>530</b>	440	(286)
Discontinued operations, net of taxes		(20)	(6)
Net income (loss)	<b>530</b>	420	(292)
Less: net (income) loss attributable to the noncontrolling interest from continuing operations	<b>(50)</b>	14	3
<b>NET INCOME (LOSS) ATTRIBUTABLE TO THE COMPANY</b>	<b>\$ 480</b>	\$ 434	(\$ 289)

The abbreviation OTTI's above means other than temporary impairment losses.  
The abbreviation OCI above means other comprehensive income (loss).

See Notes to Condensed Consolidated Financial Statements

Pacific Mutual Holding Company and Subsidiaries

## Condensed Consolidated Statements of Equity

(In Millions)	Members' Capital	Accumulated Other Comprehensive Income (Loss)		Total Members' Equity	Non- Controlling Interest	Total Equity
		Unrealized Gain (Loss) on Derivatives and Securities Available for Sale, Net	Other, Net			
<b>BALANCES, JANUARY 1, 2008</b>	<b>\$ 6,217</b>	<b>\$ 141</b>	<b>\$ 46</b>	<b>\$ 6,404</b>	<b>\$ 214</b>	<b>\$ 6,618</b>
Comprehensive loss:						
Net loss	(289)			(289)	(3)	(292)
Other comprehensive loss, net		(1,889)	(138)	(2,027)		(2,027)
Total comprehensive loss				(2,316)		(2,319)
Change in equity of noncontrolling interest					33	33
<b>BALANCES, DECEMBER 31, 2008</b>	<b>5,928</b>	<b>(1,748)</b>	<b>(92)</b>	<b>4,088</b>	<b>244</b>	<b>4,332</b>
Cumulative effect of adoption of new accounting principle, net of tax	175	(170)		5		5
Comprehensive income (loss):						
Net income (loss)	434			434	(14)	420
Other comprehensive income (loss)		1,565	56	1,621	(7)	1,614
Total comprehensive income				2,055		2,034
Change in equity of noncontrolling interest					8	8
<b>BALANCES, DECEMBER 31, 2009</b>	<b>6,537</b>	<b>(353)</b>	<b>(36)</b>	<b>6,148</b>	<b>231</b>	<b>6,379</b>
Comprehensive income (loss):						
Net income	480			480	50	530
Other comprehensive income (loss)		666	(1)	665		665
Total comprehensive income				1,145		1,195
Change in equity of noncontrolling interest					(30)	(30)
<b>BALANCES, DECEMBER 31, 2010</b>	<b>\$ 7,017</b>	<b>\$ 313</b>	<b>(\$ 37)</b>	<b>\$ 7,293</b>	<b>\$ 251</b>	<b>\$ 7,544</b>

See Notes to Condensed Consolidated Financial Statements

## Condensed Consolidated Statements of Cash Flows

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income (loss) from continuing operations	<b>\$ 530</b>	\$ 440	(\$ 286)
Adjustments to reconcile net income (loss) from continuing operations to net cash provided by operating activities:			
Net accretion on fixed maturity securities	<b>(136)</b>	(144)	(144)
Depreciation and amortization	<b>300</b>	281	259
Deferred income taxes	<b>44</b>	441	(535)
Net realized investment (gain) loss	<b>84</b>	(164)	767
Other than temporary impairments	<b>113</b>	312	584
Realized investment gain on interest in PIMCO			(109)
Net change in deferred policy acquisition costs	<b>42</b>	(235)	(192)
Interest credited to policyholder account balances	<b>1,317</b>	1,253	1,234
Net change in future policy benefits and other insurance liabilities	<b>730</b>	180	1,187
Other operating activities, net	<b>34</b>	154	(307)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES BEFORE DISCONTINUED OPERATIONS</b>	<b>3,058</b>	2,518	2,458
Net cash used in operating activities of discontinued operations		(27)	(18)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>3,058</b>	2,491	2,440
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Fixed maturity and equity securities available for sale:			
Purchases	<b>(7,185)</b>	(6,092)	(3,128)
Sales	<b>4,126</b>	1,916	2,167
Maturities and repayments	<b>2,280</b>	2,648	2,298
Repayments of mortgage loans	<b>746</b>	406	470
Fundings of mortgage loans and real estate	<b>(870)</b>	(1,434)	(1,665)
Net change in policy loans	<b>(181)</b>	411	(510)
Sale of interest in PIMCO			288
Purchases of derivative instruments	<b>(116)</b>	(20)	(12)
Terminations of derivative instruments	<b>(51)</b>	7	301
Proceeds from nonhedging derivative settlements	<b>39</b>	168	781
Payments for nonhedging derivative settlements	<b>(608)</b>	(1,653)	(142)
Net change in collateral received or pledged	<b>7</b>	(1,243)	1,029
Issuance of notes receivable	<b>(263)</b>	(603)	(1,214)
Repayments of notes receivable	<b>386</b>	673	1,382
Purchases of and advance payments on aircraft leasing portfolio	<b>(754)</b>	(561)	(694)

Pacific Mutual Holding Company and Subsidiaries

# Condensed Consolidated Statements of Cash Flows

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
<b>CASH FLOWS FROM INVESTING ACTIVITIES <i>(continued)</i></b>			
Acquisition of reinsurance business			(\$ 70)
Other investing activities, net	\$ 283	\$ 27	(270)
<b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>			
BEFORE DISCONTINUED OPERATIONS	<b>(2,161)</b>	(5,350)	1,011
Net cash provided by investing activities of discontinued operations			7
<b>NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES</b>	<b>(2,161)</b>	(5,350)	1,018
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Policyholder account balances:			
Deposits	<b>4,272</b>	8,003	7,320
Withdrawals	<b>(5,162)</b>	(7,972)	(7,602)
Net change in short-term debt	<b>(404)</b>	(260)	(52)
Issuance of long-term debt	<b>1,812</b>	1,642	335
Payments of long-term debt	<b>(1,012)</b>	(383)	(381)
Other financing activities, net	<b>(30)</b>	1	33
<b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>	<b>(524)</b>	1,031	(347)
Net change in cash and cash equivalents	<b>373</b>	(1,828)	3,111
Cash and cash equivalents, beginning of year	<b>2,060</b>	3,888	777
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<b>\$ 2,433</b>	\$ 2,060	\$ 3,888
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION</b>			
Income taxes paid (received), net	<b>\$ 94</b>	(\$ 140)	(\$ 32)
Interest paid	<b>\$ 238</b>	\$ 201	\$ 271

See Notes to Condensed Consolidated Financial Statements

## Notes to Condensed Consolidated Financial Statements

### **Note 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.

PMHC and its subsidiaries and affiliates have primary business operations consisting of life insurance, annuities, mutual funds, 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 condensed 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 is the primary beneficiary. Noncontrolling interest is primarily comprised of private equity funds. All significant intercompany transactions and balances have been eliminated in consolidation.

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 critical, 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 2009 and 2008 condensed consolidated financial statements to conform to the 2010 condensed consolidated financial statement presentation.

The Company has evaluated events subsequent to December 31, 2010 through March 7, 2011, the date the condensed consolidated financial statements were available to be issued.

**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 did 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 condensed consolidated financial statements.

Effective January 1, 2010, the Company adopted additional guidance to the Codification's Consolidation Topic whereby the Company changed the methodology it employs to evaluate if an entity is a VIE and, once identified, if a VIE should be included in the condensed consolidated financial statements. The new methodology places emphasis on the Company's ability to direct the activities that most significantly impact the VIE's financial performance. This guidance provides for enhanced disclosure requirements. The adoption of this guidance did not impact the Company's condensed consolidated financial statements, however, adoption did result in additional disclosure on the condensed consolidated statements of financial condition.

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. See Note 8 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 (loss) (OCI). Additionally, this update

provides for enhanced presentation and disclosure of OTTI of debt and equity securities in the condensed 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.

**FUTURE ADOPTION OF NEW ACCOUNTING PRONOUNCEMENTS** In October 2010, the FASB issued Accounting Standards Update (ASU) 2010-26 to the Codification's Financial Services – Insurance Topic. ASU 2010-26 significantly amends the guidance applicable to accounting for costs associated with acquiring or renewing insurance contracts. This update addresses the diversity in practice regarding the interpretation of which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral. The amendment specifies the following costs incurred in the acquisition of new and renewal contracts should be capitalized: 1) incremental direct costs of contract acquisition and 2) certain costs related directly to underwriting, policy issuance and processing, medical and inspecting, and sales force contract selling activities. This amendment also specifies that costs may only be capitalized based on successful contract acquisition efforts. Previously, insurance entities were able to capitalize costs relating to successful and unsuccessful contract acquisition efforts. The amendment is effective on January 1, 2012 and can be applied prospectively or retrospectively. The Company is currently evaluating the impact of this revised guidance on its condensed consolidated financial statements.

**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, recognized 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, which are included in other investments, 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 OTTIs. If a decline in the estimated fair value of an available for sale security is deemed to be other than temporary, the OTTI is recognized equal to the difference between the estimated fair value and net carrying amount of the security. If the OTTI for a fixed maturity security is attributable to both credit and other factors, then the OTTI is bifurcated and the non credit related portion is recognized in OCI while the credit portion is recognized as an OTTI. If the OTTI is related to credit factors only, it is recognized as an OTTI.

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.

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 are 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 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.

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, an impairment loss is recorded when the carrying amount is greater than the Company's estimated fair value of the underlying collateral of the loan. When the underlying collateral of the loan is greater than the carrying amount, the loan is not considered to have an impaired loss and no write-down is recorded. As of December 31, 2010, one loan totaling \$6 million was foreclosed upon. Since the estimated fair value of the collateral was greater than the carrying amount of the loan, no impairment loss was recorded. This loan was the only default realized during the year ended December 31, 2010. As of December 31, 2009, two loans totaling \$8 million were considered impaired, however no impairment loss was necessary as the estimated fair value of the collateral was greater than the carrying amount of the related loans.

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). Non-marketable equity securities are carried at fair value with unrealized gains or losses recognized in OCI. 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.

Real estate investments are evaluated for impairment based on the undiscounted cash flows expected to be received during the estimated holding period. When the undiscounted cash flows are less than the current carrying value of the property (gross cost less accumulated depreciation) the property is considered impaired and will be written-down to its estimated fair value. During the year ended December 31, 2010, three real estate investments were written-down for a total of \$27 million (Note 8). The Company had no real estate write-downs during the years ended December 31, 2009 and 2008.

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, changes in the estimated fair value of the hedging derivative, including amounts measured as ineffectiveness, and changes in the estimated fair value of the hedged item related to the designated risk being hedged, are reported in net realized investment gain (loss). The change in estimated 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 or pledged, in accordance with legally enforceable counterparty master netting agreements (Note 5).

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 or interest expense, which is included in operating and other expenses. 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, which is included in operating and other expenses, or interest credited to policyholder account balances over its remaining life.

**CASH AND CASH EQUIVALENTS** Cash and cash equivalents include all investments with a maturity of three months or less from purchase date.

**RESTRICTED CASH** Restricted cash primarily consists of security deposits, commitment fees, maintenance reserve 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, 2010 and 2009, the carrying value of DAC was \$4.6 billion and \$4.9 billion, respectively (Note 3).

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 3).

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 capitalized sales inducement balance included in the DAC asset was \$549 million and \$583 million as of December 31, 2010 and 2009, 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 records 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. The Company had five and four non-earning aircraft in the portfolio as of December 31, 2010 and 2009, respectively.

**POLICYHOLDER ACCOUNT BALANCES** Policyholder account balances on UL and investment-type contracts, such as funding agreements, annuities without life contingencies, 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 6). 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 with life contingencies, 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 6). Interest rates used in establishing such liabilities ranged from 0.8% to 11.0%.

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 6).

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, 2010 and 2009, 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.

**REVENUES, BENEFITS AND EXPENSES** Premiums from 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.

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 and also includes the amortization of URR. 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 by 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, 2010 and 2009, capital leases in the amount of \$5 million and \$8 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 10.

**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 condensed 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 condensed consolidated statements of financial condition. Revenue and expenses are recognized within the respective revenue and benefit and expense lines in the condensed consolidated statements of operations.

**FAIR VALUE OF FINANCIAL INSTRUMENTS** The estimated fair value of financial instruments, disclosed in Notes 4 and 8, 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.

## *Note 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 Nebraska Department of Insurance (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 the valuation of investments and certain assets and accounting for deferred income taxes on a different basis.

Pacific Life has one permitted practice approved by the NE DOI that differs 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, 2010 and 2009 did not reflect unrealized losses of \$24 million and \$29 million, respectively, with regard to this permitted practice.

In addition, Pacific Life uses an NE DOI prescribed accounting practice for certain synthetic GIC reserves that differs from statutory accounting practices adopted by the NAIC. As of December 31, 2010 and 2009, this NE DOI prescribed accounting practice resulted in statutory reserves of \$27 million and \$20 million, respectively, as opposed to statutory reserves of zero, using statutory accounting practices adopted by the NAIC.

**STATUTORY NET INCOME (LOSS) AND SURPLUS** Statutory net income (loss) of Pacific Life was

\$741 million, \$652 million and (\$1,529) million for the years ended December 31, 2010, 2009 and 2008, respectively. Statutory capital and surplus of Pacific Life was \$5,867 million and \$5,006 million as of December 31, 2010 and 2009, 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, 2010 and 2009, 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 2010 statutory results, Pacific Life could pay \$688 million in dividends in 2011 to Pacific LifeCorp without prior approval from the NE DOI, subject to the notification requirement.

During the year ended December 31, 2010, Pacific Life paid a cash dividend to Pacific LifeCorp of \$150 million. No dividends were paid during 2009. 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 2010 statutory results, PL&A could pay \$28 million in dividends to Pacific Life in 2011 without prior regulatory approval. No dividends were paid during 2010, 2009 and 2008.

**OTHER** The Company has ceded reinsurance contracts in place with a reinsurer whose financial stability has deteriorated. 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 situation and evaluate its options to deal with any further deterioration in the reinsurer's financial condition. As of December 31, 2010, statutory reserves ceded to this reinsurer amounted to \$177 million.

### *Note 3.* **DEFERRED POLICY ACQUISITION COSTS**

Components of DAC are as follows:

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
Balance, January 1	<b>\$ 4,857</b>	\$ 5,028	\$ 4,481
Cumulative pre-tax effect of adoption of new accounting principle		7	
Additions:			
Capitalized during the year	<b>662</b>	822	774
Amortization:			
Allocated to commission expenses	<b>(558)</b>	(457)	(449)
Allocated to operating expenses	<b>(146)</b>	(130)	(133)
Total amortization	<b>(704)</b>	(587)	(582)
Allocated to OCI	<b>(255)</b>	(413)	355
Balance, December 31	<b>\$ 4,560</b>	\$ 4,857	\$ 5,028

During the years ended December 31, 2010, 2009 and 2008, 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 \$34 million, \$23 million and \$20 million for the years ended December 31, 2010, 2009 and 2008, respectively. The revised EGPs also resulted in increased URR amortization of \$20 million for the year ended December 31, 2010, an immaterial decrease in URR amortization for the year ended December 31, 2009 and increased URR amortization of \$2 million for the year ended December 31, 2008.

#### Note 4. 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 of fixed maturity securities represents amortized cost adjusted for OTTI recognized in earnings and changes in the estimated fair value attributable to the hedged risk in a fair value hedge. The net carrying amount of equity securities represents cost adjusted for OTTI. See Note 8 for information on the Company's fair value measurements and disclosure.

<i>(In Millions)</i>	Net Carrying Amount	Gross Unrealized		Estimated Fair Value
		Gains	Losses	
<b>DECEMBER 31, 2010:</b>				
U.S. Treasury securities and obligations of				
U.S. government authorities and agencies	\$ 938	\$ 21	\$ 16	\$ 943
Obligations of states and political subdivisions	955	15	44	926
Foreign governments	447	50	2	495
Corporate securities	18,734	1,424	211	19,947
Residential mortgage-backed securities	5,371	144	598	4,917
Commercial mortgage-backed securities	977	50	11	1,016
Collateralized debt obligations	118	28	26	120
Other asset-backed securities	501	54	8	547
<b>Total fixed maturity securities</b>	<b>\$ 28,041</b>	<b>\$ 1,786</b>	<b>\$ 916</b>	<b>\$ 28,911</b>
Perpetual preferred securities	\$ 323	\$ 11	\$ 36	\$ 298
Other equity securities	58		1	57
<b>Total equity securities</b>	<b>\$ 381</b>	<b>\$ 11</b>	<b>\$ 37</b>	<b>\$ 355</b>

The Company has investments in perpetual preferred securities that are primarily issued by European banks. The net carrying amount and estimated fair value of the available for sale perpetual preferred securities was \$411 million and \$369 million, respectively, as of December 31, 2010. Included in these amounts are perpetual preferred securities carried in trusts with a net carrying amount and estimated fair value of \$88 million and \$71 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, 2010, 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.

<i>(In Millions)</i>	Net Carrying Amount	Gross Unrealized		Estimated Fair Value
		Gains	Losses	
Due in one year or less	\$ 892	\$ 50	\$ 1	\$ 941
Due after one year through five years	5,379	356	33	5,702
Due after five years through ten years	9,408	697	115	9,990
Due after ten years	5,395	407	124	5,678
	21,074	1,510	273	22,311
Mortgage-backed and asset-backed securities	6,967	276	643	6,600
Total fixed maturities securities	\$ 28,041	\$ 1,786	\$ 916	\$ 28,911

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 equity securities.

<i>(Dollars in Millions)</i>	Number	Total	
		Estimated Fair Value	Gross Unrealized Losses
<b>DECEMBER 31, 2010:</b>			
U.S. Treasury securities and obligations of U.S. government authorities and agencies	5	\$ 442	\$ 16
Obligations of states and political subdivisions	44	612	44
Foreign governments	9	62	2
Corporate securities	415	3,306	211
Residential mortgage-backed securities	311	2,990	598
Commercial mortgage-backed securities	21	141	11
Collateralized debt obligations	5	67	26
Other asset-backed securities	19	122	8
Total fixed maturity securities	829	7,742	916
Perpetual preferred securities	23	207	36
Other securities	31	165	17
Total other securities	54	372	53
Total	883	\$ 8,114	\$ 969
		Less than 12 Months	12 Months or Greater
		Gross	Gross

<i>(Dollars in Millions)</i>	Number	Estimated Fair Value	Unrealized Losses	Number	Estimated Fair Value	Unrealized Losses
<b>DECEMBER 31, 2010:</b>						
U.S. Treasury securities and obligations of U.S. government authorities and agencies	5	\$ 442	\$ 16			
Obligations of states and political subdivisions	32	374	16	12	\$ 238	\$ 28
Foreign governments	9	62	2			
Corporate securities	306	2,071	70	109	1,235	141
Residential mortgage-backed securities	105	167	4	206	2,823	594
Commercial mortgage-backed securities	15	52	2	6	89	9
Collateralized debt obligations				5	67	26
Other asset-backed securities	7	30	1	12	92	7
<b>Total fixed maturity securities</b>	<b>479</b>	<b>3,198</b>	<b>111</b>	<b>350</b>	<b>4,544</b>	<b>805</b>
Perpetual preferred securities	6	12	1	17	195	35
Other securities	5	70	2	26	95	15
<b>Total other securities</b>	<b>11</b>	<b>82</b>	<b>3</b>	<b>43</b>	<b>290</b>	<b>50</b>
<b>Total</b>	<b>490</b>	<b>\$ 3,280</b>	<b>\$ 114</b>	<b>393</b>	<b>\$ 4,834</b>	<b>\$ 855</b>

The Company has evaluated fixed maturity and other securities with gross unrealized losses and has determined that the unrealized losses are temporary. 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 presents non-agency residential mortgage-backed securities (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, 2010.

(Dollars in Millions) Rating	Net Carrying Amount	Estimated Fair Value	Rating as % of Net Carrying Amount	Vintage Breakdown				
				2004 and Prior	2005	2006	2007	2008 and After
<b>Prime RMBS:</b>								
AAA	\$ 635	\$ 634	21%	18%	3%			
AA	113	107	4%	3%		1%		
A	121	119	4%	1%	2%	1%		
BAA	31	28	1%		1%			
BA and below	2,073	1,762	70%	3%	22%	31%	14%	
<b>Total</b>	<b>\$ 2,973</b>	<b>\$ 2,650</b>	<b>100%</b>	<b>25%</b>	<b>28%</b>	<b>33%</b>	<b>14%</b>	<b>0%</b>
<b>Alt-A RMBS:</b>								
AAA	\$ 54	\$ 50	6%	6%				
AA	27	27	3%	1%	1%	1%		
BAA	26	24	3%	1%		2%		
BA and below	747	560	88%		10%	26%	52%	
<b>Total</b>	<b>\$ 854</b>	<b>\$ 661</b>	<b>100%</b>	<b>8%</b>	<b>11%</b>	<b>29%</b>	<b>52%</b>	<b>0%</b>
<b>Sub-prime RMBS:</b>								
AAA	\$ 212	\$ 199	52%	52%				
AA	92	80	23%	23%				
A	21	14	5%	5%				
BA and below	83	67	20%	1%	17%	1%	1%	
<b>Total</b>	<b>\$ 408</b>	<b>\$ 360</b>	<b>100%</b>	<b>81%</b>	<b>17%</b>	<b>1%</b>	<b>1%</b>	<b>0%</b>
<b>CMBS:</b>								
AAA	\$ 842	\$ 888	86%	59%	3%		14%	10%
AA	65	66	7%	4%				3%
A	42	38	4%	4%				
BA	28	24	3%				3%	
<b>Total</b>	<b>\$ 977</b>	<b>\$ 1,016</b>	<b>100%</b>	<b>67%</b>	<b>3%</b>	<b>0%</b>	<b>17%</b>	<b>13%</b>

Pacific Life is a member of the Federal Home Loan Bank (FHLB) of Topeka. As of December 31, 2010, the Company has received advances of \$1.5 billion from the FHLB of Topeka and has issued funding agreements to the FHLB of Topeka in connection with its institutional investment products. The funding agreement liabilities are included in policyholder account balances. Fixed maturity securities and cash equivalents with an estimated fair value of \$1.7 billion as of December 31, 2010 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, 2010, the Company holds \$78 million of FHLB of Topeka stock, which is recorded in other investments.

PL&A is a member of FHLB of San Francisco. As of December 31, 2010, no assets are pledged as collateral. As of December 31, 2010, the Company holds FHLB of San Francisco stock with an estimated fair value of \$28 million, which is recorded in other investments.

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

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
Fixed maturity securities	<b>\$ 1,538</b>	\$ 1,477	\$ 1,489
Equity securities	<b>19</b>	20	23
Mortgage loans	<b>337</b>	297	289
Real estate	<b>95</b>	94	87
Policy loans	<b>214</b>	229	223
Partnerships and joint ventures	<b>119</b>	(77)	21
Other	<b>1</b>	16	34
Gross investment income	<b>2,323</b>	2,056	2,166
Investment expense	<b>167</b>	159	137
Net investment income	<b>\$ 2,156</b>	\$ 1,897	\$ 2,029

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

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
Fixed maturity securities:			
Gross gains on sales	<b>\$ 181</b>	\$ 61	\$ 107
Gross losses on sales	<b>(36)</b>	(19)	(44)
Total fixed maturity securities	<b>145</b>	42	63
Equity securities:			
Gross gains on sales	4		1
Gross losses on sales		(11)	
Total equity securities	<b>4</b>	(11)	1
Trading securities	<b>12</b>	20	(22)
Real estate	<b>21</b>		
Variable annuity GLB embedded derivatives (including reinsurance contracts)	<b>185</b>	2,211	(2,775)
Variable annuity GLB policy fees	<b>208</b>	147	108
Variable annuity derivatives – interest rate swaps		(104)	402
Variable annuity derivatives – total return swaps	<b>(534)</b>	(1,542)	646
Equity put options	<b>(159)</b>	(672)	853
Synthetic GIC policy fees	<b>30</b>	25	15
Other derivatives	<b>8</b>	38	(78)
Other	<b>(4)</b>	10	20
Total	<b>(\$ 84)</b>	\$ 164	(\$ 767)

The table below summarizes the OTTI by investment type:

Recorded                      Included

<i>(In Millions)</i>	in Earnings	in OCI	Total
<b>YEAR ENDED DECEMBER 31, 2010:</b>			
Corporate securities	\$ 10		\$ 10
RMBS	64	\$ 215	279
Collateralized debt obligations	1		1
OTTIs – fixed maturity and equity securities	75	215	290
Real estate	27		27
Other investments	11		11
<b>Total OTTIs</b>	<b>\$ 113</b>	<b>\$ 215</b>	<b>\$ 328</b>
<b>YEAR ENDED DECEMBER 31, 2009:</b>			
Corporate securities <sup>(1)</sup>	\$ 63	\$ 2	\$ 65
RMBS	117	315	432
Collateralized debt obligations	66	13	79
Perpetual preferred securities	26		26
OTTIs – fixed maturity and equity securities	272	330	602
Other investments	40		40
<b>Total OTTIs</b>	<b>\$ 312</b>	<b>\$ 330</b>	<b>\$ 642</b>

<sup>(1)</sup> Included are \$29 million of OTTI recognized in earnings on perpetual preferred securities carried in trusts.

#### *Note 5. 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 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 condensed consolidated statement of financial condition. 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**

Notional Amount

<i>(In Millions)</i> DECEMBER 31,	2010	2009
Foreign currency interest rate swaps	<b>\$ 4,917</b>	\$ 5,099
Interest rate swaps	<b>2,727</b>	3,910
Forward starting interest rate swaps	<b>1,140</b>	1,060

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 condensed 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

<i>(In Millions)</i> DECEMBER 31,	Notional Amount	
	2010	2009
Interest rate swaps	<b>\$ 1,579</b>	\$ 1,658
Foreign currency interest rate swaps	<b>13</b>	13

#### DERIVATIVES NOT DESIGNATED AS HEDGING INSTRUMENTS

<i>(In Millions)</i> DECEMBER 31,	Notional Amount	
	2010	2009
Variable annuity GLB embedded derivatives	<b>\$ 37,147</b>	\$ 36,408
Variable annuity GLB reinsurance contracts	<b>15,117</b>	14,878
Variable annuity derivatives – total return swaps	<b>2,891</b>	4,456
Equity put options	<b>5,285</b>	5,267
EIUL embedded derivatives	<b>538</b>	331
S&P call options	<b>483</b>	306
Synthetic GICs	<b>22,402</b>	23,993
Foreign currency interest rate swaps	<b>424</b>	398
Interest rate swaps	<b>1,609</b>	2,438
Other	<b>455</b>	541

**CONDENSED CONSOLIDATED FINANCIAL STATEMENT IMPACT** Derivative instruments are recorded on the Company's condensed consolidated statements of financial condition at estimated 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.

**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, 2010 was \$110 million. The maximum exposure to any single counterparty was \$17 million at December 31, 2010.

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 were to fall below a specified level, as defined within each counterparty master agreement or, in most cases, if one of the rating agencies ceased to provide an insurer financial strength rating, the counterparty could terminate the master agreement with

payment due based on the estimated fair value of the underlying derivatives. As of December 31, 2010, Pacific Life's insurer financial strength ratings were above the specified level.

The Company enters into collateral arrangements with derivative counterparties, which require both the pledging and accepting of collateral when the net estimated fair value of the underlying derivatives reaches a pre-determined threshold. Certain of these arrangements include credit-contingent provisions that provide for a reduction of these thresholds in the event of downgrades in the credit ratings of the Company and/or the counterparty. If Pacific Life's insurer financial strength rating were to fall below a specific investment grade credit rating, the counterparties to the derivative instruments could request immediate and ongoing full 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, 2010, is \$329 million for which the Company has posted collateral of \$203 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, 2010, the Company would have been required to post an additional \$29 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.

#### Note 6. POLICYHOLDER LIABILITIES

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

##### POLICYHOLDER ACCOUNT BALANCES

<i>(In Millions)</i> DECEMBER 31,	2010	2009
Universal life	<b>\$ 20,098</b>	\$ 19,298
Annuity and deposit liabilities	<b>8,335</b>	7,109
Funding agreements	<b>4,618</b>	5,240
GICs	<b>2,025</b>	2,337
<b>Total</b>	<b>\$ 35,076</b>	\$ 33,984

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

##### FUTURE POLICY BENEFITS

<i>(In Millions)</i> DECEMBER 31,	2010	2009
Annuity reserves	<b>\$ 4,926</b>	\$ 4,960
Life insurance	<b>679</b>	618
Variable annuity GLB embedded derivatives	<b>542</b>	754
URR	<b>510</b>	734
Policy benefits payable	<b>456</b>	342
Closed Block liabilities	<b>303</b>	306
Other	<b>25</b>	24
<b>Total</b>	<b>\$ 7,441</b>	\$ 7,738

#### Note 7. DEBT

Debt consists of the following:

<i>(In Millions)</i> DECEMBER 31,	2010	2009
<b>Short-term debt:</b>		
Revolving credit facilities		\$ 220
Credit facility recourse only to ACG		105
College Savings Bank repurchase agreements	<b>\$ 135</b>	214
<b>Total short-term debt</b>	<b>\$ 135</b>	<b>\$ 539</b>
<b>Long-term debt:</b>		
Surplus notes	<b>\$ 1,150</b>	\$ 1,150
Senior notes	<b>1,047</b>	600
Fair value adjustment for derivative hedging activities	<b>84</b>	(13)
Deferred gains from derivative hedging activities	<b>270</b>	277
		(13)
<b>Non-recourse long-term debt:</b>		
Debt recourse only to ACG	<b>2,499</b>	1,636
ACG non-recourse debt	<b>621</b>	761
Other non-recourse debt	<b>120</b>	121
ACG VIE debt	<b>1,587</b>	1,975
Other VIE debt	<b>5</b>	2
<b>Total long-term debt</b>	<b>\$ 7,383</b>	<b>\$ 6,509</b>

#### *Note 8.* **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 fixed maturity 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 certain 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 table presents, by fair value hierarchy level, the Company's financial assets and liabilities that are carried at fair value as of December 31, 2010.

<i>(In Millions)</i>	Level 1	Level 2	Level 3	Gross Derivatives Fair Value	Netting Adjustments <sup>(1)</sup>	Total
<b>Assets:</b>						
U.S. Treasury securities and obligations of						
U.S. government authorities and agencies		\$ 943				<b>\$ 943</b>
Obligations of states and political subdivisions		886	\$ 40			<b>926</b>
Foreign governments		425	70			<b>495</b>
Corporate securities		18,319	1,628			<b>19,947</b>
RMBS		3,849	1,068			<b>4,917</b>
CMBS		762	254			<b>1,016</b>
Collateralized debt obligations		5	115			<b>120</b>
Other asset-backed securities		267	280			<b>547</b>
<b>Total fixed maturity securities</b>		<b>25,456</b>	<b>3,455</b>			<b>28,911</b>
Perpetual preferred securities			286	12		<b>298</b>
Other equity securities	\$ 56			1		<b>57</b>
<b>Total equity securities</b>	<b>56</b>	<b>286</b>	<b>13</b>			<b>355</b>
Trading securities <sup>(2)</sup>	91	192	66			<b>349</b>
Other investments			191			<b>191</b>
<b>Derivatives:</b>						
Interest rate swaps		207	6	\$ 213	(\$ 112)	<b>101</b>
Foreign currency interest rate swaps		256		256	(266)	<b>(10)</b>
Equity derivatives			322	322	(95)	<b>227</b>
Embedded derivatives			25	25		<b>25</b>
Other		6	5	11	(32)	<b>(21)</b>
<b>Total derivatives</b>		<b>469</b>	<b>358</b>	<b>827</b>	<b>(505)</b>	<b>322</b>
Separate account assets <sup>(3)</sup>	55,438	123	100			<b>55,661</b>
<b>Total</b>	<b>\$ 55,585</b>	<b>\$ 26,526</b>	<b>\$ 4,183</b>	<b>\$ 827</b>	<b>(\$ 505)</b>	<b>\$ 85,789</b>
<b>Liabilities:</b>						
<b>Derivatives:</b>						
Interest rate swaps		\$ 246		\$ 246	(\$ 112)	<b>\$ 134</b>
Foreign currency interest rate swaps		442		442	(266)	<b>176</b>
Equity derivatives			\$ 102	102	(95)	<b>7</b>
Embedded derivatives			620	620		<b>620</b>
Other			23	23	(32)	<b>(9)</b>
<b>Total</b>		<b>\$ 688</b>	<b>\$ 745</b>	<b>\$ 1,433</b>	<b>(\$ 505)</b>	<b>\$ 928</b>

<sup>(1)</sup> Netting adjustments represent the impact of offsetting asset and liability positions on the condensed consolidated statement of financial condition 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 condensed 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 tables above differ from the amounts presented in the condensed 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.

**NONRECURRING FAIR VALUE MEASUREMENTS** Certain assets are measured at estimated fair value on a nonrecurring basis and are not included in the table presented above. The amounts below relate to certain investments measured at estimated fair value during 2010 and still held at December 31, 2010.

<i>(In Millions)</i>	Carrying Value Prior to Measurement	Estimated Fair Value After Measurement	Net Investment Loss
Real estate investments	<b>\$ 69</b>	\$ 42	(\$ 27)
Aircraft	<b>24</b>	20	(4)

#### Note 9. INCOME TAXES

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

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
Current	<b>\$ 6</b>	(\$ 417)	\$ 196
Deferred	<b>44</b>	441	(535)
Provision (benefit) for income taxes from continuing operations	<b>50</b>	24	(339)
Benefit from income taxes from discontinued operations		(11)	(3)
Total	<b>\$ 50</b>	\$ 13	(\$ 342)

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 condensed consolidated financial statements is as follows:

<i>(In Millions)</i> YEARS ENDED DECEMBER 31,	2010	2009	2008
Provision (benefit) for income taxes at the statutory rate	<b>\$ 203</b>	\$ 163	(\$ 219)
Separate account dividends received deduction	<b>(106)</b>	(93)	(107)
LIHTC and foreign tax credits	<b>(18)</b>	(19)	(31)
Other	<b>(29)</b>	(27)	18
Provision (benefit) for income taxes from continuing operations	<b>\$ 50</b>	\$ 24	(\$ 339)

*Note 10. COMMITMENTS AND CONTINGENCIES*

**COMMITMENTS** The Company has outstanding commitments to make investments primarily in fixed maturity securities, mortgage loans, limited partnerships and other investments, as follows:

*(In Millions)* YEARS ENDING DECEMBER 31:

2011	\$ 606
2012 through 2015	647
2016 and thereafter	46
Total	\$ 1,299

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 \$11 million, \$10 million and \$12 million for the years ended December 31, 2010, 2009 and 2008, 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 \$11 million, related to an office lease that has been assigned to the buyer. Aggregate minimum future commitments are as follows:

*(In Millions)* YEARS ENDING DECEMBER 31:

2011	\$ 12
2012 through 2015	30
2016 and thereafter	2
Total	\$ 44

ACG entered into a sale leaseback transaction, the subject of which was two commercial aircraft on long-term lease to a U.S. airline. As a result of this transaction, ACG has committed to two operating leases

expiring December 2025 and in turn benefits from operating leases on the two sale leaseback aircraft which expire July 2021 and April 2024. Aggregate minimum future lease commitments and minimum rentals to be received in the future are as follows:

<i>(In Millions)</i> YEARS ENDING DECEMBER 31,	Minimum Future Commitments	Minimum Rentals to be Received
2011	\$ 11	\$ 9
2012 through 2015	23	37
2016 and thereafter	64	63
<b>Total</b>	<b>\$ 98</b>	<b>\$ 109</b>

As of December 31, 2010, ACG has commitments with major aircraft manufacturers and other third-parties to purchase aircraft at an estimated delivery price of \$6,125 million with delivery from 2011 through 2017. These purchase commitments may be funded:

- up to \$1,205 million in less than one year,
- an additional \$2,297 million in one to three years,
- an additional \$1,699 million in three to five years, and
- an additional \$417 million thereafter.

As of December 31, 2010, deposits related to these agreements totaled \$507 million and are included in other assets.

In connection with the reinsurance of no lapse guarantee rider benefits ceded from Pacific Life to PAR Vermont, 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, 2010, the letter of credit issued from this facility for PAR Bermuda was cancelled. In addition, as of December 31, 2010, a letter of credit was issued for PAR Vermont totaling \$355 million. Pacific LifeCorp guarantees the obligations of PAR Vermont under the letter of credit agreement.

In connection with the acquisition of Pacific Life Re Limited (PLR), Pacific LifeCorp provided a guarantee for the performance of certain obligations of PLR. In addition, Pacific LifeCorp provided indemnification for certain matters, as set forth in the purchase agreement. As stated in the guarantee agreement, if PLR is unable to meet its current obligations under unaffiliated reinsurance agreements, Pacific LifeCorp shall guarantee payment on any past, present and future obligations of PLR. On March 29, 2010, Pacific Life entered into an agreement with PLR to guarantee the performance of unaffiliated reinsurance obligations of PLR. PLR will pay Pacific Life a fee for its guarantee. For the year ended December 31, 2010, Pacific Life earned \$2 million under the agreement for its guarantee. This guarantee is secondary to the guarantee provided by Pacific LifeCorp and would only be triggered in the event of nonperformance by both PLR and Pacific LifeCorp. Management believes that any additional obligations, if any, related to either of the guarantee agreements are not likely to have a material adverse effect on the Company's condensed consolidated financial statements.

**CONTINGENCIES – LITIGATION** The Company is a respondent in a number of 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 condensed consolidated financial position. The

Company believes adequate provision has been made in its condensed consolidated financial statements for all probable and estimable losses for litigation claims against the Company.

**CONTINGENCIES – OTHER** In connection with the sale of certain broker-dealer subsidiaries, 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. 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 condensed consolidated financial statements.

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 condensed 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.

Some of ACG's asset purchase agreements 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 condensed consolidated financial statements.

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 5 for discussion of contingencies related to derivative instruments.

*Pacific Mutual Holding Company and Subsidiaries*  
**Independent Auditors' Report**

We have audited the consolidated statements of financial condition of Pacific Mutual Holding Company and Subsidiaries (the Company) as of December 31, 2010 and 2009, and the related consolidated statements of operations, equity and cash flows for each of the three years in the period ended December 31, 2010. Such consolidated financial statements and our report thereon dated March 7, 2011, expressing an unqualified opinion (which are not included herein) are included in the Company's annual filings made with the Insurance Department of the State of Nebraska. The accompanying condensed consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on such condensed consolidated financial statements in relation to the complete consolidated financial statements.

In our opinion, the information set forth in the accompanying condensed consolidated financial statements of financial condition of Pacific Mutual Holding Company and Subsidiaries as of December 31, 2010 and 2009, the related condensed consolidated statements of operations, equity and cash flows for each of the three years in the period ended December 31, 2010, is stated fairly in all material respects in relation to the consolidated financial statements from which it has been derived.

As discussed in Note 1 to the condensed consolidated financial statements the Company changed its method of accounting and reporting for variable interest entities as required by guidance adopted in 2010, as well as for other than temporary impairments and noncontrolling interest as required by accounting guidance adopted in 2009.

Deloitte & Touche LLP  
Costa Mesa, California  
March 7, 2011

# Corporate Information



## Statement of Management's Responsibility

The management of Pacific Mutual Holding Company and Subsidiaries (the Company) assumes responsibility for the preparation of the accompanying condensed consolidated financial statements and for all other information in this 2010 Report to Members. This responsibility includes maintaining the integrity and objectivity of all such information. The financial statements include amounts that are based on management's best estimates and judgments. The accompanying condensed consolidated financial statements are derived from consolidated financial statements that have been audited by Deloitte & Touche LLP, independent auditors. Their audits were conducted in accordance with auditing standards generally accepted in the United States of America and included consideration of internal controls and tests of transactions as part of planning and performing their audits.

The Company is committed to maintaining internal controls that provide reasonable assurance that assets are safeguarded and that transactions are properly executed and recorded in accordance with management's authorization. Internal controls are supported by appropriate divisions of responsibilities and separation of duties, specified delegations of authority, established policies and procedures that are clearly communicated, including a code of business conduct to foster a strong ethical climate, and the careful selection, training, and development of employees. A responsibility telephone line is available to all employees to anonymously report suspected violations of the code of business conduct. An internal audit department independently assesses the adequacy and effectiveness of internal controls and recommends possible improvements thereto. Management considers the recommendations of the internal auditors and Deloitte & Touche LLP concerning internal controls and takes appropriate actions to respond to these recommendations.

The Board of Directors of Pacific Mutual Holding Company has an audit committee composed entirely of external, independent directors who meet regularly with management, the internal auditors, and the independent auditors. Both the internal auditors and the independent auditors have direct access to and meet with the audit committee on a regular basis (or at a minimum at each audit committee meeting), without management representatives present, to discuss the scope and results of their audits, their views on the adequacy of internal controls, and the quality of financial reporting.

Finally, management also maintains policies to encourage a climate in which the Company's affairs are conducted in accordance with the highest standards of personal and professional conduct.

**James T. Morris**

Chairman, President and Chief Executive Officer

**Khanh T. Tran**

Executive Vice President, Chief Financial Officer and  
Chief Investment Officer

March 7, 2011

# Directors

## **Douglas D. Abbey** <sup>1,2</sup>

Founder  
AMB Property Corporation

## **Mariann Byerwalter** <sup>1,2</sup>

Chairman  
JDN Corporate Advisory LLC

## **Sharon A. Cheever** <sup>3</sup>

Senior Vice President and  
General Counsel  
Pacific Life Insurance Company

## **Dwight W. Decker** <sup>1</sup>

Retired Chairman and  
Chief Executive Officer  
Conexant Systems, Inc.

## **John Gottschalk** <sup>1</sup>

Chairman  
Omaha World-Herald Company

## **Julia S. Gouw** <sup>1,2</sup>

President and Chief Operating Officer  
East West Bank

## **Jane M. Guon** <sup>3</sup>

Vice President and Secretary  
Pacific Life Insurance Company

## **Lawrence F. Harr** <sup>3</sup>

Partner  
Lamson, Dugan and Murray, LLP

## **James T. Morris** <sup>1,2,3</sup>

Chairman, President and  
Chief Executive Officer  
Pacific Life Insurance Company

## **J. Fernando Niebla** <sup>2</sup>

Managing Partner  
International Technology Partners, LLC

## **Susan Westerberg Prager** <sup>1</sup>

Executive Director  
Chief Executive Officer  
Association of American Law Schools  
Professor of Law and Dean, Emeritus  
UCLA School of Law

## **J. Michael Shepherd** <sup>1,2</sup>

Chairman and Chief Executive Officer  
BancWest Corporation

## **Thomas C. Sutton** <sup>1,2</sup>

Retired Chairman and  
Chief Executive Officer  
Pacific Life Insurance Company

## **William S. Thompson** <sup>2</sup>

Retired Chief Executive Officer  
PIMCO

## **Khanh T. Tran** <sup>3</sup>

Executive Vice President,  
Chief Financial Officer and  
Chief Investment Officer  
Pacific Life Insurance Company

## **Dean A. Yoost** <sup>2</sup>

Financial Advisor

<sup>1</sup> Director of Pacific Mutual Holding Company

<sup>2</sup> Director of Pacific LifeCorp

<sup>3</sup> Director of Pacific Life Insurance Company

# Senior Management

**James T. Morris, FSA**  
Chairman, President and  
Chief Executive Officer

**Michael A. Bell**  
Executive Vice President  
Life Insurance Division

**Mary Ann Brown, FSA**  
Executive Vice President  
Corporate Development,  
Risk Management and Technology

**Dewey P. Bushaw**  
Executive Vice President  
Retirement Solutions Division

**Michael S. Robb, CRE, CRA**  
Executive Vice President  
Real Estate Division

**Khanh T. Tran**  
Executive Vice President,  
Chief Financial Officer and  
Chief Investment Officer

**Edward R. Byrd**  
Senior Vice President and  
Chief Accounting Officer

**Joseph E. Celentano**  
Senior Vice President  
Enterprise Risk Management

**Sharon A. Cheever**  
Senior Vice President and  
General Counsel

**Martha Gates, ACS**  
Senior Vice President, Operations  
Life Insurance Division

**Thomas Gibbons**  
Senior Vice President  
Tax and Enterprise Consulting

**Adrian S. Griggs**  
Senior Vice President  
Finance and Risk Management  
Retirement Solutions Division

**Robert G. Haskell**  
Senior Vice President  
Brand Management and Public Affairs

**Denis P. Kalscheur**  
Senior Vice President and Treasurer

**Henry M. McMillan, PhD, FSA**  
Senior Vice President and  
Chief Risk Officer

**Tod Nasser**  
Senior Vice President  
Portfolio Management

**Andrew Oleksiw**  
Senior Vice President  
Business Development

**Richard J. Schindler, CLU, FLMI**  
Senior Vice President and  
Chief Marketing Officer  
Life Insurance Division

**Carol R. Sudbeck**  
Senior Vice President  
Human Resources and Facilities

**Philip A. Teeter**  
Senior Vice President  
Technology and Operations  
Retirement Solutions Division

**Dawn M. Trautman**  
Senior Vice President  
Information Technology and  
Strategic Planning  
Life Insurance Division

**Chris van Mierlo**  
Senior Vice President, Sales and  
Chief Marketing Officer  
Retirement Solutions Division

# Contact Information

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[www.PacificMutual.com](http://www.PacificMutual.com)

**Pacific Life Insurance Company/  
Pacific Life & Annuity Company**  
700 Newport Center Drive  
Newport Beach, CA 92660-6397  
(800) 800-7646, ext. 3011 / (949) 219-3011  
Email: [Info@PacificLife.com](mailto:Info@PacificLife.com)  
[www.PacificLife.com](http://www.PacificLife.com)  
[www.PacificLifeandAnnuity.com](http://www.PacificLifeandAnnuity.com)

**Investment Management**  
(800) 800-7646, ext. 3310

**Real Estate Division**  
(800) 800-7646, ext. 4763

**Retirement Solutions Division**  
(800) 722-4448

**Life Insurance Division**  
45 Enterprise  
Aliso Viejo, CA 92656-2601  
(800) 800-7681, ext. 6000 / (949) 420-6000

## Principal Subsidiaries

**Aviation Capital Group Corp.**  
610 Newport Center Drive, Suite 1400  
Newport Beach, CA 92660-6465  
(949) 219-4600  
[www.AviationCapitalGroup.com](http://www.AviationCapitalGroup.com)

**College Savings Bank**  
5 Vaughn Drive, Suite 100  
Princeton, NJ 08540-6313  
(800) 888-2723 / (609) 987-3700  
[www.CollegeSavings.com](http://www.CollegeSavings.com)

**Pacific Asset Management**  
(800) 800-7646, ext. 1656 / (949) 219-1656  
[www.PAM.PacificLife.com](http://www.PAM.PacificLife.com)

**Pacific Life Re Limited**  
Tower Bridge House  
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London E1W 1BA  
+44 (0)20 7709 1700  
[www.PacificLifeRe.com](http://www.PacificLifeRe.com)

**Pacific Select Distributors, Inc.**  
(800) 800-7646, ext. 3881 / (949) 219-3881

## **The Annual Meeting of Members of *Pacific Mutual Holding Company***

(ALL LIFE INSURANCE AND ANNUITY POLICYHOLDERS OF PACIFIC LIFE INSURANCE COMPANY)

The Annual Meeting of Members of Pacific Mutual Holding Company will be held at 11:30 a.m. on May 25, 2011, at 700 Newport Center Drive, Newport Beach, California, for the purpose of the election of directors and for such other business as may properly come before the meeting.

Jane M. Guon, Secretary



# PACIFIC MUTUAL

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[www.PacificMutual.com](http://www.PacificMutual.com)



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