

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

The registrant meets the conditions set forth in General Instructions I (1)(a) and (b) of Form 10-K and is therefore filing this form with the reduced disclosure format.

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2008

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

Commission file number: 0-31248

ALLSTATE LIFE INSURANCE COMPANY
(Exact name of registrant as specified in its charter)

Illinois 36-2554642
(State of Incorporation) (I.R.S. Employer Identification No.)

3100 Sanders Road, Northbrook, Illinois 60062
(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: (847) 402-5000

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value \$227.00 per share

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer	Non-accelerated filer	Smaller reporting company
<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
(Do not check if a smaller reporting company)			

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

None of the common equity of the registrant is held by non-affiliates.

Therefore, the aggregate market value of the common equity held by non-affiliates of the registrant is zero.

AS OF MARCH 18, 2009, THE REGISTRANT HAD 23,800 COMMON SHARES, \$227 PAR VALUE, OUTSTANDING, ALL OF WHICH ARE HELD BY ALLSTATE INSURANCE COMPANY.

ALLSTATE LIFE INSURANCE COMPANY
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DECEMBER 31, 2008

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* Omitted pursuant to General Instruction I(2) of Form 10-K

PART I

ITEM 1. BUSINESS

Allstate Life Insurance Company was organized in 1957 as a stock life insurance company under the laws of the State of Illinois. Allstate Life Insurance Company, together with its subsidiaries, provides life insurance, retirement and investment products for individual and institutional customers. It conducts substantially all of its operations directly or through wholly owned United States subsidiaries. In this document, we refer to Allstate Life Insurance Company as "Allstate Life" or "ALIC" and to Allstate Life and its wholly owned subsidiaries as the "Allstate Life Group" or the "Company."

Allstate Life is a wholly owned subsidiary of Allstate Insurance Company, a stock property-liability insurance company organized under the laws of the State of Illinois. All of the outstanding stock of Allstate Insurance Company is owned by Allstate Insurance Holdings, LLC, which is wholly owned by The Allstate Corporation, a publicly owned holding company incorporated under the laws of the State of Delaware. In this document, we refer to Allstate Insurance Company as "AIC" and to The Allstate Corporation and its consolidated subsidiaries as "Allstate", the "Parent Group" or the "Corporation". The Allstate Corporation is the largest publicly held personal lines insurer in the United States. Widely known through the "You're In Good Hands With Allstate(R)" slogan, Allstate is reinventing protection and retirement to help individuals in approximately 17

million households protect what they have today and better prepare for tomorrow. Customers can access Allstate products and services such as auto insurance and homeowners insurance through more than 14,000 exclusive Allstate agencies and financial representatives in the United States and Canada. Allstate is the 2nd largest personal property and casualty insurer in the United States on the basis of 2007 statutory direct premiums earned. In addition, according to A.M. Best, it is the nation's 16th largest issuer of life insurance business on the basis of 2007 ordinary life insurance in force and 17th largest on the basis of 2007 statutory admitted assets.

The Parent Group has four business segments, one of which is Allstate Financial. Allstate Financial, which is not a separate legal entity, is comprised of the Allstate Life Group together with American Heritage Life Insurance Company, the Allstate Bank and other Parent Group subsidiaries that are not part of the Allstate Life Group. This document describes the Allstate Life Group. It does not describe the entire group of companies that form the Allstate Financial segment of the Parent Group.

To achieve its goals in 2009, Allstate is focused on three priorities: protect Allstate's financial strength, build customer loyalty, and continue reinventing protection and retirement for the consumer.

In this annual report on Form 10-K, we occasionally refer to statutory financial information. All domestic United States insurance companies are required to prepare statutory-basis financial statements. As a result, industry data is available that enables comparisons between insurance companies, including competitors that are not subject to the requirement to prepare financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP"). We frequently use industry publications containing statutory financial information to assess our competitive position.

PRODUCTS AND DISTRIBUTION

The Allstate Life Group provides life insurance, retirement and investment products to individual and institutional customers. Our principal individual products are fixed annuities, including deferred, immediate and indexed; and interest-sensitive, traditional and variable life insurance. We also distribute variable annuities through our bank distribution partners, however, this product is fully reinsured with an unaffiliated entity. Our principal institutional product is funding agreements backing medium-term notes. The table on page 2 lists our major distribution channels, with the associated products and targeted customers.

As the table indicates, we sell products to individuals through multiple intermediary distribution channels, including Allstate exclusive agencies and exclusive financial specialists, independent agents, banks, broker-dealers, and specialized structured settlement brokers. We have distribution relationships with over 60% of the 25 largest banks, a number of regional brokerage firms and many independent broker-dealers. We sell products through independent agents affiliated with approximately 160 master brokerage agencies. We sell funding agreements to unaffiliated trusts used to back medium-term notes.

DISTRIBUTION CHANNELS, PRODUCTS AND TARGET CUSTOMERS

DISTRIBUTION
 CHANNEL
 PRIMARY
 PRODUCTS
 TARGET
 CUSTOMERS -

 ALLSTATE
 EXCLUSIVE
 AGENCIES
 Term life
 insurance
 Middle
 market

consumers(1)
with
Interest-
sensitive
life
insurance
retirement
and family
financial
(Allstate
exclusive
agents
Variable
life
insurance
protection
needs and
Allstate
exclusive
Deferred
fixed
annuities
(including
financial
specialists)
indexed and
market value
adjusted
"MVA")
Immediate
fixed
annuities
INDEPENDENT
AGENTS Term

life
insurance
Mass
market(2)
and mass
affluent
(through
master
brokerage
Interest-
sensitive
life
insurance
consumers(3)

with
retirement
agencies)
Variable
life
insurance
and
financial
protection
needs
Deferred
fixed
annuities
(including
indexed and
MVA)
Immediate
fixed
annuities
BANKS
Deferred
fixed
annuities
(including
indexed
Middle
market
consumers
with and
MVA)
retirement
needs Single
premium

fixed life
insurance
Variable
annuities -
fully
reinsured
with an
unaffiliated
entity
BROKER-
DEALERS
Deferred
fixed
annuities
(including
indexed Mass
market and
mass
affluent and
MVA)
consumers
with
retirement
needs Single
premium
variable
life
insurance
STRUCTURED
SETTLEMENT
Structured
settlement
annuities
Typically
used to fund
or annuitize
ANNUITY
BROKERS
large claims
or
litigation
settlements
BROKER-
DEALERS
Funding
agreements
backing
medium-term
notes
Institutional
and
individual
investors
(Funding
agreements)

- - - - -
- (1) Consumers with \$50,000 - \$125,000 in household income
 - (2) Consumers with \$50,000 - \$75,000 in household income
 - (3) Consumers with \$75,000 - \$125,000 in household income

Allstate exclusive agencies and exclusive financial specialists also sell the following non-proprietary products: mutual funds, variable annuities and long-term care insurance.

In connection with an initiative to lower operating expenses beginning in 2009, we plan to improve efficiency and narrow the focus of product offerings to better serve the needs of everyday Americans.

COMPETITION

We compete on a wide variety of factors, including the scope of our distribution systems, the type of our product offerings, the recognition of our brands, our financial strength and ratings, our differentiated product features and prices, and the level of customer service that we provide. With regard to funding agreements, we compete principally on the basis of our financial strength and ratings.

The market for life insurance, retirement and investment products continues to be highly fragmented and competitive. As of December 31, 2008, there were

approximately 500 groups of life insurance companies in the United States, most of which offered one or more similar products. According to A.M. Best, as of December 31, 2007, the Allstate Life Group is the nation's 16th largest issuer of life insurance and related business on the basis of 2007 ordinary life insurance in force and 17th largest on the basis of 2007 statutory admitted assets. In addition, because many of these products include a savings or investment component, our competition includes domestic and foreign securities firms, investment advisors, mutual funds, banks and other financial institutions. Competitive pressure continues to grow due to several factors, including cross marketing alliances between unaffiliated businesses, as well as consolidation activity in the financial services industry.

GEOGRAPHIC MARKETS

We sell life insurance, retirement and investment products throughout the United States. The Allstate Life Group is authorized to sell various types of these products in all 50 states, the District of Columbia, Puerto Rico, the U.S. Virgin Islands and Guam. We also sell funding agreements in the United States.

The following table reflects, in percentages, the principal geographic distribution of statutory premiums and annuity considerations for the Allstate Life Group for the year ended December 31, 2008, based on information contained in statements filed with state insurance departments.

Delaware	37.7%
California	6.6%
Florida	6.0%
New York	5.8%

Approximately 99 percent of the statutory premiums and annuity considerations generated in Delaware represent deposits received in connection with funding agreements sold to trusts domiciled in Delaware. No other jurisdiction accounted for more than 5 percent of the statutory premiums and annuity considerations.

REGULATION

The Allstate Life Group is subject to extensive regulation, primarily at the state level. The method, extent and substance of such regulation varies by state but generally has its source in statutes that establish standards and requirements for conducting the business of insurance and that delegate regulatory authority to a state regulatory agency. In general, such regulation is intended for the protection of those who purchase or use insurance products. These rules have a substantial effect on our business and relate to a wide variety of matters including insurance company licensing and examination, agent licensing, price setting, trade practices, policy forms, accounting methods, the nature and amount of investments, claims practices, participation in guaranty funds, reserve adequacy, insurer solvency, transactions with affiliates, the payment of dividends, and underwriting standards. Some of these matters are discussed in more detail below. For a discussion of statutory financial information, see Note 14 of the Consolidated Financial Statements. For a discussion of regulatory contingencies, see Note 11 of the Consolidated Financial Statements. Notes 11 and 14 are incorporated in this Part I, Item 1 by reference.

In recent years, the state insurance regulatory framework has come under increased federal scrutiny. Legislation that would provide for federal chartering of insurance companies has been proposed. In addition, state legislators and insurance regulators continue to examine the appropriate nature and scope of state insurance regulation. We cannot predict whether any specific state or federal measures will be adopted to change the nature or scope of the regulation of the insurance business or what effect any such measures would have on the Allstate Life Group.

AGENT AND BROKER COMPENSATION. In recent years, several states considered new legislation or regulations regarding the compensation of agents and brokers by insurance companies. The proposals ranged in nature from new disclosure requirements to new duties on insurance agents and brokers in dealing with customers. New disclosure requirements have been imposed in certain circumstances upon some agents and brokers in several states.

LIMITATIONS ON DIVIDENDS BY INSURANCE SUBSIDIARIES. Allstate Life may receive dividends from time to time from its subsidiaries. When received, these dividends represent a source of cash from which Allstate Life may meet some of its obligations. If a subsidiary is an insurance company, its ability to pay

dividends may be restricted by state laws regulating insurance companies. For additional information regarding those restrictions, see Note 14 of the Consolidated Financial Statements.

GUARANTY FUNDS. Under state insurance guaranty fund laws, insurers doing business in a state can be assessed, up to prescribed limits, in order to cover certain obligations of insolvent insurance companies.

INVESTMENT REGULATION. Our insurance subsidiaries are subject to regulations that require investment portfolio diversification and that limit the amount of investment in certain categories. Failure to comply with these rules leads to the treatment of non-conforming investments as non-admitted assets for purposes of measuring statutory surplus. Further, in some instances, these rules require divestiture of non-conforming investments.

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VARIABLE LIFE INSURANCE, VARIABLE ANNUITIES AND REGISTERED FIXED ANNUITIES. The sale and administration of variable life insurance, variable annuities and registered fixed annuities with market value adjustment features are subject to extensive regulatory oversight at the federal and state level, including regulation and supervision by the Securities and Exchange Commission and the Financial Industry Regulatory Authority ("FINRA").

BROKER-DEALERS, INVESTMENT ADVISORS AND INVESTMENT COMPANIES. The Allstate Life Group entities that operate as broker-dealers, registered investment advisors and investment companies are subject to regulation and supervision by the Securities and Exchange Commission, FINRA and/or, in some cases, state securities administrators.

PRIVACY REGULATION. Federal law and the laws of some states require financial institutions to protect the security and confidentiality of customer information and to notify customers about their policies and practices relating to collection and disclosure of customer information and their policies relating to protecting the security and confidentiality of that information. Federal law and the laws of some states also regulate disclosures of customer information. Congress, state legislatures and regulatory authorities are expected to consider additional regulation relating to privacy and other aspects of customer information.

EMPLOYEES AND OTHER SHARED SERVICES

The Allstate Life Group has no employees. Instead, we primarily use the services of employees of Allstate Insurance Company, our direct parent. We also make use of other services and facilities provided by Allstate Insurance Company and other members of the Parent Group. These services and facilities include space rental, utilities, building maintenance, human resources, investment management, finance, information technology and legal services. We reimburse our affiliates for these services and facilities under a variety of agreements.

OTHER INFORMATION

"Allstate" is one of the most recognized brand names in the United States. We use the names "Allstate," "Lincoln Benefit Life" and variations of these names extensively in our business, along with related logos and slogans, such as "Goods Hands." Our rights in the United States to these names, logos and slogans continue so long as we continue to use them in commerce. Most of these service marks are the subject of renewable U.S. and/or foreign service mark registrations. We believe that these service marks are important to our business and we intend to maintain our rights to them through continued use.

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ITEM 1A. RISK FACTORS

This document contains "forward-looking statements" that anticipate results based on our estimates, assumptions and plans that are subject to uncertainty. These statements are made subject to the safe-harbor provisions of the Private Securities Litigation Reform Act of 1995. We assume no obligation to update any forward-looking statements as a result of new information or future events or developments.

These forward-looking statements do not relate strictly to historical or current facts and may be identified by their use of words like "plans," "seeks," "expects," "will," "should," "anticipates," "estimates," "intends," "believes," "likely," "targets" and other words with similar meanings. These statements may address, among other things, our strategy for growth, product development, investment results, regulatory approvals, market position, expenses, financial results, litigation and reserves. We believe that these statements are based on

reasonable estimates, assumptions and plans. However, if the estimates, assumptions or plans underlying the forward-looking statements prove inaccurate or if other risks or uncertainties arise, actual results could differ materially from those communicated in these forward-looking statements.

In addition to the normal risks of business, we are subject to significant risks and uncertainties, including those listed below, which apply to us as an insurer and a provider of other financial services. These risks constitute our cautionary statements under the Private Securities Litigation Reform Act of 1995 and readers should carefully review such cautionary statements as they identify certain important factors that could cause actual results to differ materially from those in the forward-looking statements and historical trends. These cautionary statements are not exclusive and are in addition to other factors discussed elsewhere in this document, in our filings with the Securities and Exchange Commission ("SEC") or in materials incorporated therein by reference.

CHANGES IN UNDERWRITING AND ACTUAL EXPERIENCE COULD MATERIALLY AFFECT PROFITABILITY AND FINANCIAL CONDITION

Our product pricing includes long-term assumptions regarding investment returns, mortality, morbidity, persistency and operating costs and expenses of the business. Management establishes target returns for each product based upon these factors and the average amount of capital that the Company must hold to support in-force contracts taking into account rating agencies and regulatory requirements. We monitor and manage our pricing and overall sales mix to achieve target new business returns on a portfolio basis, which could result in the discontinuation of products or distribution relationships and a decline in sales. Profitability from new business emerges over a period of years depending on the nature and life of the product and is subject to variability as actual results may differ from pricing assumptions.

Our profitability depends on the adequacy of investment spreads, the management of market and credit risks associated with investments, the sufficiency of premiums and contract charges to cover mortality and morbidity benefits, the persistency of policies to ensure recovery of acquisition expenses, and the management of operating costs and expenses within anticipated pricing allowances. Legislation and regulation of the insurance marketplace and products could also affect our profitability and financial condition.

CHANGES IN RESERVE ESTIMATES MAY ADVERSELY AFFECT OUR OPERATING RESULTS

Reserve for life-contingent contract benefits is computed on the basis of long-term actuarial assumptions of future investment yields, mortality, morbidity, policy terminations and expenses. We periodically review the adequacy of these reserves on an aggregate basis and if future experience differs significantly from assumptions, adjustments to reserves and amortization of deferred policy acquisition costs ("DAC") may be required which could have a material adverse effect on our operating results.

CHANGES IN MARKET INTEREST RATES MAY LEAD TO A SIGNIFICANT DECREASE IN THE SALES AND PROFITABILITY OF SPREAD-BASED PRODUCTS

Our ability to manage our spread-based products, such as fixed annuities and institutional products, is dependent upon maintaining profitable spreads between investment yields and interest crediting rates. When market interest rates decrease or remain at relatively low levels, proceeds from investments that have matured or have been prepaid or sold may be reinvested at lower yields, reducing investment spread. Lowering interest crediting rates in such an environment can partially offset decreases in investment yield on some products. However, these changes could be limited by market conditions, regulatory minimum rates or contractual minimum rate guarantees on many contracts and may not match the timing or magnitude of changes in asset yields. Decreases in the rates offered on products could make those products less attractive, leading to lower sales and/or changes in the level of policy loans, surrenders and withdrawals. Non-parallel shifts in interest rates, such as increases in short-term rates without accompanying increases in medium- and long-term rates, can influence customer demand for fixed annuities, which could impact the level and profitability of new customer deposits. Increases in market interest rates can also have

negative effects, for example by increasing the attractiveness of other investments to our customers, which can lead to higher surrenders at a time when fixed income investment asset values are lower as a result of the increase in interest rates. This could lead to the sale of fixed income securities at a loss. For certain products, principally fixed annuity and interest-sensitive life products, the earned rate on assets could lag behind rising market yields. We may react to market conditions by increasing crediting rates, which could narrow spreads and reduce profitability. Unanticipated

surrenders could result in accelerated amortization of DAC or affect the recoverability of DAC and thereby increase expenses and reduce profitability.

CHANGES IN ESTIMATES OF PROFITABILITY ON INTEREST-SENSITIVE LIFE, FIXED ANNUITIES AND OTHER INVESTMENT PRODUCTS MAY ADVERSELY AFFECT OUR PROFITABILITY AND FINANCIAL CONDITION THROUGH INCREASED AMORTIZATION OF DAC

DAC related to interest-sensitive life, fixed annuities and other investment contracts is amortized in proportion to actual historical gross profits and estimated future gross profits ("EGP") over the estimated lives of the contracts. The principal assumptions for determining the amount of EGP are investment returns, including capital gains and losses on assets supporting contract liabilities, interest crediting rates to contractholders, and the effects of persistency, mortality, expenses, and hedges if applicable. Updates to these assumptions (commonly referred to as "DAC unlocking") could adversely affect our profitability and financial condition. In 2008, DAC unlocking resulted in increased amortization of DAC of \$329 million.

NARROWING THE FOCUS OF OUR PRODUCT OFFERINGS AND REDUCING OUR CONCENTRATION IN FIXED ANNUITIES AND FUNDING AGREEMENTS MAY ADVERSELY AFFECT REPORTED RESULTS

Due to the current capital market conditions, we have been pursuing strategies to narrow our product offerings and reduce our concentration in fixed annuities and funding agreements. Lower new sales of these products, as well as our ongoing risk mitigation and return optimization programs, could negatively impact investment portfolio levels, complicate settlement of expiring contracts including forced sales of assets with unrealized capital losses, impact DAC amortization, and affect goodwill impairment testing and insurance reserves deficiency testing.

A LOSS OF KEY PRODUCT DISTRIBUTION RELATIONSHIPS COULD MATERIALLY AFFECT SALES

Certain products are distributed under agreements with other members of the financial services industry that are not affiliated with us. Termination of one or more of these agreements due to, for example, a change in control of one of these distributors, could have a detrimental effect on sales.

CHANGES IN TAX LAWS MAY DECREASE SALES AND PROFITABILITY OF PRODUCTS AND FINANCIAL CONDITION

Under current federal and state income tax law, certain products we offer, primarily life insurance and annuities, receive favorable tax treatment. This favorable treatment may give certain of our products a competitive advantage over noninsurance products. Congress from time to time considers legislation that would reduce or eliminate the favorable policyholder tax treatment currently applicable to life insurance and annuities. Congress also considers proposals to reduce the taxation of certain products or investments that may compete with life insurance and annuities. Legislation that increases the taxation on insurance products or reduces the taxation on competing products could lessen the advantage or create a disadvantage for certain of our products making them less competitive. Such proposals, if adopted, could have a material adverse effect on our profitability and financial condition or ability to sell such products and could result in the surrender of some existing contracts and policies. In addition, changes in the federal estate tax laws could negatively affect the demand for the types of life insurance used in estate planning.

RISKS RELATING TO INVESTMENTS

WE ARE SUBJECT TO MARKET RISK AND DECLINES IN CREDIT QUALITY WHICH MAY ADVERSELY IMPACT INVESTMENT INCOME AND CAUSE ADDITIONAL REALIZED LOSSES

Although we continually reevaluate our proactive risk mitigation and return optimization programs, we remain subject to the risk that we will incur losses due to adverse changes in equity prices, interest rates or foreign currency exchange rates. Our primary market risk exposures are to changes in interest rates and, to a lesser degree, equity prices and changes in foreign currency exchange rates. In addition, we are subject to potential declines in credit quality, either related to issues specific to certain industries or to a general weakening in the economy. Although to some extent we use derivative financial instruments to manage these risks, the effectiveness of such instruments is subject to the same risks.

A decline in market interest rates could have an adverse effect on our investment income as we invest cash in new investments that may yield less than the portfolio's average rate. In a declining interest rate environment, borrowers may prepay or redeem securities more quickly than expected as they seek to refinance at lower rates. A

decline could also lead us to purchase longer-term or riskier assets in order to obtain adequate investment yields resulting in a duration gap when compared to the duration of liabilities. An increase in market interest rates could have an adverse effect on the value of our investment portfolio by decreasing the fair values of the fixed income securities that comprise a substantial majority of our investment portfolio. A decline in the quality of our investment portfolio as a result of adverse economic conditions or otherwise could cause additional realized losses on securities, including realized losses relating to equity and derivative strategies.

DETERIORATING FINANCIAL PERFORMANCE ON SECURITIES COLLATERALIZED BY MORTGAGE LOANS AND COMMERCIAL MORTGAGE LOANS MAY LEAD TO WRITE-DOWNS

Changes in mortgage delinquency or recovery rates, declining real estate prices, changes in credit or bond insurer strength ratings and the quality of service provided by service providers on securities in our portfolios could lead us to determine that write-downs are appropriate in the future.

THE IMPACT OF OUR INVESTMENT STRATEGIES MAY BE ADVERSELY AFFECTED BY DEVELOPMENTS IN THE INVESTMENT MARKETS

The impact of our investment portfolio risk mitigation and return optimization programs and enterprise asset allocation actions may be adversely affected by unexpected developments in the investment markets. For example, derivative contracts, when entered into, may result in coverage that is not as effective as intended.

CONCENTRATION OF OUR INVESTMENT PORTFOLIOS IN ANY PARTICULAR SEGMENT OF THE ECONOMY MAY HAVE ADVERSE EFFECTS ON OUR OPERATING RESULTS AND FINANCIAL CONDITION

The concentration of our investment portfolios in any particular industry, collateral types, group of related industries or geographic sector could have an adverse effect on our investment portfolios and consequently on our results of operations and financial condition. Events or developments that have a negative impact on any particular industry, group of related industries or geographic region may have a greater adverse effect on the investment portfolios to the extent that the portfolios are concentrated rather than diversified.

THE DETERMINATION OF THE AMOUNT OF REALIZED CAPITAL LOSSES RECORDED FOR IMPAIRMENTS OF OUR INVESTMENTS IS HIGHLY SUBJECTIVE AND COULD MATERIALLY IMPACT OUR OPERATING RESULTS AND FINANCIAL CONDITION

The determination of the amount of realized capital losses recorded for impairments vary by investment type and is based upon our periodic evaluation and assessment of known and inherent risks associated with the respective asset class. Such evaluations and assessments are revised as conditions change and new information becomes available. Management updates its evaluations regularly and reflects changes in realized capital gains and losses from impairments in operating results as such evaluations are revised. There can be no assurance that our management has accurately assessed the level of or amounts recorded for impairments taken in our financial statements. Furthermore, additional impairments may need to be recorded in the future. Historical trends may not be indicative of future impairments. For example, the amortized cost or cost of our fixed income and equity securities is adjusted for impairments in value deemed to be other than temporary in the period in which the determination is made. The assessment of whether impairments have occurred is based on management's case-by-case evaluation of the underlying reasons for the decline in fair value.

THE DETERMINATION OF THE FAIR VALUE OF OUR FIXED INCOME AND EQUITY SECURITIES RESULTS IN UNREALIZED NET CAPITAL GAINS AND LOSSES AND IS HIGHLY SUBJECTIVE AND COULD MATERIALLY IMPACT OUR OPERATING RESULTS AND FINANCIAL CONDITION

In determining fair value we generally utilize market transaction data for the same or similar instruments. The degree of management judgment involved in determining fair values is inversely related to the availability of market observable information. The fair value of financial assets and financial liabilities may differ from the amount actually received to sell an asset or the amount paid to transfer a liability in an orderly transaction between market participants at the measurement date. Moreover, the use of different valuation assumptions may have a material effect on the financial assets' and financial liabilities' fair values. The difference between amortized cost or cost and fair value, net of deferred income taxes, certain DAC, certain deferred sales inducement costs ("DSI"), and certain reserves for life-contingent contract benefits, is reflected as a component of accumulated other comprehensive income in shareholder's equity. As of December 31, 2008, total unrealized net capital losses was \$6.70 billion. In the last 10 years, our quarterly net unrealized capital gains and losses have ranged from a \$4.35 billion net unrealized capital gain at June 30, 2003 to a \$6.70 billion net unrealized capital loss at December 31, 2008. Changing market conditions could materially effect the determination of the fair value of our securities and unrealized net capital gains and losses

could vary significantly. Determining fair value is highly subjective and could materially impact our operating results and financial condition.

RISKS RELATING TO THE INSURANCE INDUSTRY

OUR FUTURE RESULTS ARE DEPENDENT IN PART ON OUR ABILITY TO SUCCESSFULLY OPERATE IN AN INSURANCE INDUSTRY THAT IS HIGHLY COMPETITIVE

The insurance industry is highly competitive. Our competitors include other insurers and, because many of our products include a savings or investment component, securities firms, investment advisers, mutual funds, banks and other financial institutions. Many of our competitors have well-established national reputations and market similar products. Because of the competitive nature of the insurance industry, including competition for producers such as exclusive and independent agents, there can be no assurance that we will continue to effectively compete with our industry rivals, or that competitive pressures will not have a material adverse effect on our business, operating results or financial condition. Furthermore, certain competitors operate using a mutual insurance company structure and therefore, may have dissimilar profitability and return targets. Our ability to successfully operate may also be impaired if we are not effective in filling critical leadership positions, in developing the talent and skills of our human resources, in assimilating new executive talent into our organization, or in deploying human resource talent consistently with our business goals.

DIFFICULT CONDITIONS IN THE ECONOMY GENERALLY COULD ADVERSELY AFFECT OUR BUSINESS AND OPERATING RESULTS

Economists now believe the United States economy has entered into a recessionary period and are projecting significant negative macroeconomic trends, including widespread job losses, higher unemployment, lower consumer spending, continued declines in home prices and substantial increases in delinquencies on consumer debt, including defaults on home mortgages. Moreover, recent disruptions in the financial markets, particularly the reduced availability of credit and tightened lending requirements, have impacted the ability of borrowers to refinance loans at more affordable rates. We cannot predict the length and severity of a recession, but as with most businesses, we believe a longer or more severe recession could have an adverse effect on our business and results of operations.

A general economic slowdown could adversely affect us in the form of consumer behavior and pressure on our investment portfolio. Consumer behavior could include decreased demand for our products. Holders of some of our life insurance and annuity products may engage in an elevated level of discretionary withdrawals of contractholder funds. Our investment portfolio could be adversely affected as a result of deteriorating financial and business conditions affecting the issuers of the securities in our investment portfolio.

THERE CAN BE NO ASSURANCE THAT ACTIONS OF THE U.S. FEDERAL GOVERNMENT, FEDERAL RESERVE AND OTHER GOVERNMENTAL AND REGULATORY BODIES FOR THE PURPOSE OF STABILIZING THE FINANCIAL MARKETS AND STIMULATING THE ECONOMY WILL ACHIEVE THE INTENDED EFFECT

In response to the financial crises affecting the banking system, the financial markets and the broader economy, the U.S. federal government, the Federal Reserve and other governmental and regulatory bodies have taken or are considering taking action to address such conditions including, among other things, purchasing mortgage-backed and other securities from financial institutions, investing directly in banks, thrifts and bank and savings and loan holding companies and increasing federal spending to stimulate the economy. There can be no assurance as to what impact such actions will have on the financial markets or on economic conditions. Such continued volatility and economic deterioration could materially and adversely affect our business, financial condition and results of operations.

LOSSES FROM LITIGATION MAY BE MATERIAL TO OUR OPERATING RESULTS OR CASH FLOWS AND FINANCIAL CONDITION

As is typical for a large company, we are involved in a substantial amount of litigation, including class action litigation challenging a range of company practices and coverage provided by our insurance products. In the event of an unfavorable outcome in one or more of these matters, the ultimate liability may be in excess of amounts currently reserved and may be material to our operating results or cash flows for a particular quarter or annual period and to our financial condition.

WE ARE SUBJECT TO EXTENSIVE REGULATION AND POTENTIAL FURTHER RESTRICTIVE REGULATION MAY INCREASE OUR OPERATING COSTS AND LIMIT OUR GROWTH

As insurance companies, broker-dealers, investment advisers and/or investment companies, many of our subsidiaries are subject to extensive laws and regulations. These laws and regulations are complex and subject to change. Moreover, they are administered and enforced by a number of different governmental authorities, including state insurance regulators, state securities administrators, the SEC, Financial Industry Regulatory Authority, the U.S. Department of Justice, and state attorneys general, each of which exercises a degree of interpretive latitude. Consequently, we are subject to the risk that compliance with any particular regulator's or enforcement authority's interpretation of a legal issue may not result in compliance with another's interpretation of the same issue, particularly when compliance is judged in hindsight. In addition, there is risk that any particular regulator's or

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enforcement authority's interpretation of a legal issue may change over time to our detriment, or that changes in the overall legal environment may, even absent any particular regulator's or enforcement authority's interpretation of a legal issue changing, cause us to change our views regarding the actions we need to take from a legal risk management perspective, thus necessitating changes to our practices that may, in some cases, limit our ability to grow and improve the profitability of our business. Furthermore, in some cases, these laws and regulations are designed to protect or benefit the interests of a specific constituency rather than a range of constituencies. For example, state insurance laws and regulations are generally intended to protect or benefit purchasers or users of insurance products. In many respects, these laws and regulations limit our ability to grow and improve the profitability of our business.

In recent years, the state insurance regulatory framework has come under public scrutiny and members of Congress have discussed proposals to provide for federal chartering of insurance companies. We can make no assurances regarding the potential impact of state or federal measures that may change the nature or scope of insurance regulation.

REINSURANCE MAY BE UNAVAILABLE AT CURRENT LEVELS AND PRICES, WHICH MAY LIMIT OUR ABILITY TO WRITE NEW BUSINESS

Market conditions beyond our control determine the availability and cost of the reinsurance we purchase. No assurances can be made that reinsurance will remain continuously available to us to the same extent and on the same terms and rates as are currently available. If we were unable to maintain our current level of reinsurance or purchase new reinsurance protection in amounts that we consider sufficient and at prices that we consider acceptable, we would have to either accept an increase in our exposure risk, reduce our insurance writings, or develop or seek other alternatives.

REINSURANCE SUBJECTS US TO THE CREDIT RISK OF OUR REINSURERS AND MAY NOT BE ADEQUATE TO PROTECT US AGAINST LOSSES ARISING FROM CEDED INSURANCE, WHICH COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR OPERATING RESULTS AND FINANCIAL CONDITION

The collectability of reinsurance recoverables is subject to uncertainty arising from a number of factors, including changes in market conditions, whether insured losses meet the qualifying conditions of the reinsurance contract and whether reinsurers, or their affiliates, have the financial capacity and willingness to make payments under the terms of a reinsurance treaty or contract. Our inability to collect a material recovery from a reinsurer could have a material adverse effect on our operating results and financial condition.

THE CONTINUED THREAT OF TERRORISM AND ONGOING MILITARY ACTIONS MAY ADVERSELY AFFECT THE LEVEL OF CLAIM LOSSES WE INCUR AND THE VALUE OF OUR INVESTMENT PORTFOLIO

The continued threat of terrorism, both within the United States and abroad, and ongoing military and other actions and heightened security measures in response to these types of threats, may cause significant volatility and losses from declines in the equity markets and from interest rate changes in the United States, Europe and elsewhere, and result in loss of life, disruptions to commerce and reduced economic activity. Some of the assets in our investment portfolio may be adversely affected by declines in the equity markets and reduced economic activity caused by the continued threat of terrorism. We seek to mitigate the potential impact of terrorism on our commercial mortgage portfolio by limiting geographical concentrations in key metropolitan areas and by requiring terrorism insurance to the extent that it is commercially available. Additionally, in the event that terrorist acts occur, we could be adversely affected, depending on the nature of the event.

A DOWNGRADE IN OUR FINANCIAL STRENGTH RATINGS MAY HAVE AN ADVERSE EFFECT ON OUR COMPETITIVE POSITION, THE MARKETABILITY OF OUR PRODUCT OFFERINGS, AND OUR

Financial strength ratings are important factors in establishing the competitive position of insurance companies and generally have an effect on an insurance company's business. On an ongoing basis, rating agencies review the financial performance and condition of insurers and could downgrade or change the outlook on an insurer's ratings due to, for example, a change in an insurer's statutory capital; a change in a rating agency's determination of the amount of risk-adjusted capital required to maintain a particular rating; an increase in the perceived risk of an insurer's investment portfolio; a reduced confidence in management or a host of other considerations that may or may not be under the insurer's control. The current insurance financial strength ratings of the Company are A+, AA- and A1 from A.M. Best, Standard & Poor's and Moody's, respectively. The current insurance financial strength ratings of AIC are A+, AA- and Aa3 from A.M. Best, Standard & Poor's and Moody's, respectively. Because all of these ratings are subject to continuous review, the retention of these ratings cannot be assured. A downgrade in any of these ratings could have a material adverse effect on our sales, our competitiveness, the marketability of our product offerings, and our liquidity, operating results and financial condition.

ADVERSE CAPITAL AND CREDIT MARKET CONDITIONS MAY SIGNIFICANTLY AFFECT OUR ABILITY TO MEET LIQUIDITY NEEDS OR OUR ABILITY TO OBTAIN CREDIT ON ACCEPTABLE TERMS

The capital and credit markets have been experiencing extreme volatility and disruption. In some cases, the markets have exerted downward pressure on the availability of liquidity and credit capacity. In the event that we need access to additional capital to pay our operating expenses, make payments on our indebtedness, pay for capital expenditures or fund acquisitions, our ability to obtain such capital may be limited and the cost of any such capital may be significant. Our access to additional financing will depend on a variety of factors such as market conditions, the general availability of credit, the overall availability of credit to our industry, our credit ratings and credit capacity, as well as lenders' perception of our long- or short-term financial prospects. Similarly, our access to funds may be impaired if regulatory authorities or rating agencies take negative actions against us. If a combination of these factors were to occur, our internal sources of liquidity may prove to be insufficient, and in such case, we may not be able to successfully obtain additional financing on favorable terms.

CHANGES IN ACCOUNTING STANDARDS ISSUED BY THE FINANCIAL ACCOUNTING STANDARDS BOARD ("FASB") OR OTHER STANDARD-SETTING BODIES MAY ADVERSELY AFFECT OUR FINANCIAL STATEMENTS

Our financial statements are subject to the application of generally accepted accounting principles, which are periodically revised, interpreted and/or expanded. Accordingly, we are required to adopt new guidance or interpretations, or could be subject to existing guidance as we enter into new transactions, which may have a material adverse effect on our results of operations and financial condition that is either unexpected or has a greater impact than expected. For a description of changes in accounting standards that are currently pending and, if known, our estimates of their expected impact, see Note 2 of the consolidated financial statements.

THE CHANGE IN OUR UNRECOGNIZED TAX BENEFIT DURING THE NEXT 12 MONTHS IS SUBJECT TO UNCERTAINTY

As required by FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes", which was adopted as of January 1, 2007, we have disclosed our estimate of net unrecognized tax benefits and the reasonably possible increase or decrease in its balance during the next 12 months. However, actual results may differ from our estimate for reasons such as changes in our position on specific issues, developments with respect to the governments' interpretations of income tax laws or changes in judgment resulting from new information obtained in audits or the appeals process.

THE REALIZATION OF DEFERRED TAX ASSETS IS SUBJECT TO UNCERTAINTY

The realization of our deferred tax assets, net of valuation allowances, is based on our assumption that we will be able to fully utilize the deductions that are ultimately recognized for tax purposes. However, actual results may differ from our assumptions if adequate levels of taxable income are not attained.

THE OCCURRENCE OF EVENTS UNANTICIPATED IN OUR DISASTER RECOVERY SYSTEMS AND MANAGEMENT CONTINUITY PLANNING COULD IMPAIR OUR ABILITY TO CONDUCT BUSINESS EFFECTIVELY

In the event of a disaster such as a natural catastrophe, an industrial accident, a terrorist attack or war, events unanticipated in our disaster recovery systems could have an adverse impact on our ability to conduct business and on our results of operations and financial condition, particularly if those events affect our computer-based data processing, transmission, storage and retrieval systems. In the event that a significant number of our managers could be unavailable in the event of a disaster, our ability to effectively conduct our business could be severely compromised.

CHANGING CLIMATE CONDITIONS MAY ADVERSELY AFFECT OUR FINANCIAL CONDITION, PROFITABILITY OR CASH FLOWS

Allstate recognizes the scientific view that the world is getting warmer. To the extent that climate change impacts mortality rates and those changes do not match the long-term mortality assumptions in our product pricing, we would be impacted.

LOSS OF KEY VENDOR RELATIONSHIPS COULD AFFECT OUR OPERATIONS

We rely on services and products provided by many vendors in the United States and abroad. These include, for example, vendors of computer hardware and software and vendors of services such as human resource benefits management services. In the event that one or more of our vendors suffers a bankruptcy or otherwise becomes unable to continue to provide products or services, we may suffer operational impairments and financial losses.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

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ITEM 2. PROPERTIES

Our home office is part of the Parent Group's home office complex in Northbrook, Illinois. As of December 31, 2008, the complex consists of several buildings totaling approximately 2.3 million square feet of office space on a 250-acre site. In addition, we operate from various administrative, data processing, claims handling and other support facilities.

All of the facilities from which we operate are owned or leased by our direct parent, Allstate Insurance Company, except for office space in Lincoln, Nebraska that is leased by Lincoln Benefit Life Company, a wholly owned subsidiary of ALIC, for general operations, file storage and information technology. Expenses associated with facilities owned or leased by Allstate Insurance Company are allocated to us on both a direct and an indirect basis, depending on the nature and use of each particular facility. We believe that these facilities are suitable and adequate for our current operations.

The locations out of which the Parent Group exclusive agencies operate in the U.S. are normally leased by the agencies as lessees.

ITEM 3. LEGAL PROCEEDINGS

Information required for Item 3 is incorporated by reference to the discussion under the heading "Regulation" and under the heading "Legal and regulatory proceedings and inquiries" in Note 11 of the consolidated financial statements.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

No established public trading market exists for Allstate Life's common stock. All of its outstanding common stock is owned by its parent, Allstate Insurance Company ("AIC"). All of the outstanding common stock of AIC is owned by Allstate Insurance Holdings, LLC, which is wholly owned by The Allstate Corporation.

The Company did not pay dividends on its common stock in 2008. In 2007, Allstate Life paid the following amounts to AIC in the aggregate on the dates specified as dividends on its common stock:

(\$ IN
MILLIONS)
PAYMENT
DATE
AGGREGATE

AMOUNT
September
24, 2007
\$ 85
December
17, 2007
251
December
21, 2007
389

For additional information on dividends, including restrictions on the payment of dividends by Allstate Life and its subsidiaries, see the Limitations on Dividends by Insurance Subsidiaries subsection of the "Regulation" section of Item 1. Business of this Form 10-K and the discussion under the heading "Dividends" in Note 14 of our consolidated financial statements, which are incorporated herein by reference.

ITEM 6. SELECTED FINANCIAL DATA.

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
5-YEAR SUMMARY OF SELECTED FINANCIAL DATA

(\$ IN
MILLIONS)
2008 2007
2006 2005
2004 -----

CONSOLIDATED
OPERATING
RESULTS
Premiums \$
585 \$ 502 \$
576 \$ 474 \$
637 Contract
charges 911
942 1,009
1,079 961 Net
investment
income 3,720
4,205 4,057
3,707 3,260
Realized
capital gains
and losses
(3,052) (197)
(79) 19 (11)
Total
revenues
2,164 5,452
5,563 5,279
4,847 (Loss)
income before
cumulative
effect of
change in
accounting
principle,
after-tax
(1,690) 412
428 417 356
Cumulative
effect of
change in
accounting
principle,
after-tax --
-- -- --
(175) Net
(loss) income
(1,690) 412
428 417 181

CONSOLIDATED
 FINANCIAL
 POSITION
 Total
 investments \$
 59,772 \$
 72,414 \$
 74,160 \$
 72,756 \$
 69,689 Total
 assets 81,946
 96,117 98,758
 95,022 90,401
 Reserve for
 life-
 contingent
 contract
 benefits and
 contractholder
 funds 69,036
 73,062 72,769
 70,071 65,142
 Long-term
 debt/surplus
 notes due to
 related
 parties 650
 200 206 181
 104
 Shareholder's
 equity 2,209
 4,763 5,498
 6,008 6,309

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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OVERVIEW

The following discussion highlights significant factors influencing the consolidated financial position and results of operations of Allstate Life Insurance Company (referred to in this document as "we", "our", "us", the "Company" or "ALIC"). It should be read in conjunction with the 5-year summary of selected financial data, consolidated financial statements and related notes found under Part II, Item 6 and Item 8 contained herein. We operate as a single segment entity, based on the manner in which we use financial information to evaluate business performance and to determine the allocation of resources.

We are focused on three priorities in 2009: protecting our financial strength, building customer loyalty, and continue reinventing protection and retirement for the consumer.

The most important factors we monitor to evaluate the financial condition and performance of our company include:

- For operations: premiums and deposits, benefit and investment spread, amortization of deferred policy acquisition costs, expenses, operating income, net income, invested assets, and new business returns;
- For investments: credit quality/experience, realized capital gains and losses, investment income, unrealized capital gains and losses,

- stability of long-term returns, total returns, cash flows, and asset and liability duration; and
- For financial condition: liquidity, our financial strength ratings, operating leverage, debt leverage, and return on equity.

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APPLICATION OF CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to adopt accounting policies and make estimates and assumptions that affect amounts reported in the consolidated financial statements. The most critical estimates include those used in determining:

- Fair Value of Financial Assets and Financial Liabilities
- Impairment of Fixed Income and Equity Securities
- Deferred Policy Acquisition Costs ("DAC") Amortization
- Reserve for Life-Contingent Contract Benefits Estimation

In applying these policies, management makes subjective and complex judgments that frequently require estimates about matters that are inherently uncertain. Many of these policies, estimates and related judgments are common in the insurance and financial services industries; others are specific to our businesses and operations. It is reasonably likely that changes in these estimates could occur from period to period and result in a material impact on our consolidated financial statements.

A brief summary of each of these critical accounting estimates follows. For a more detailed discussion of the effect of these estimates on our consolidated financial statements, and the judgments and assumptions related to these estimates, see the referenced sections of this document. For a complete summary of our significant accounting policies, see Note 2 of the consolidated financial statements.

FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES Statement of Financial Accounting Standards No. 157, FAIR VALUE MEASUREMENTS ("SFAS No. 157"), is effective for fiscal years beginning after November 15, 2007. We adopted the provisions of SFAS No. 157 as of January 1, 2008 for financial assets and financial liabilities that are measured at fair value. SFAS No. 157:

- Defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establishes a framework for measuring fair value;
- Establishes a three-level hierarchy for fair value measurements based upon the transparency of inputs to the valuation as of the measurement date;
- Expands disclosures about financial instruments measured at fair value.

We categorize our financial assets and financial liabilities measured at fair value based on the observability of inputs to the valuation techniques, into a three-level fair value hierarchy as follows:

LEVEL 1: Financial assets and financial liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that we can access.

LEVEL 2: Financial assets and financial liabilities whose values are based on the following:

- (a) Quoted prices for similar assets or liabilities in active markets;
- (b) Quoted prices for identical or similar assets or liabilities in non-active markets; or
- (c) Valuation models whose inputs are observable, directly or indirectly, for substantially the full term of the asset or liability.

LEVEL 3: Financial assets and financial liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs may reflect our estimates of the assumptions that market participants would use in valuing the financial assets and financial liabilities.

Observable inputs are those used by market participants in valuing

financial instruments that are developed based on market data obtained from independent sources. In the absence of sufficient observable inputs, unobservable inputs reflect our estimates of the assumptions market participants would use in valuing financial assets and financial liabilities and are developed based on the best information available in the circumstances. The degree of management judgment involved in determining fair values is inversely related to the availability of market observable information.

To distinguish among the categories, we consider the frequency of completed transactions such as daily trading for equity securities. If inputs used to measure a financial instrument fall within different levels of the fair value hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the

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entire instrument. Certain financial assets are not carried at fair value on a recurring basis, including investments such as mortgage loans, limited partnership interests, bank loans and policy loans. Accordingly, such investments are only included in the fair value hierarchy disclosure when the investment is subject to remeasurement at fair value after initial recognition and the resulting measurement is reflected in the consolidated financial statements. In addition, equity options embedded in fixed income securities are not disclosed in the hierarchy with free-standing derivatives, as the embedded derivatives are presented as combined instruments in fixed income securities.

We are responsible for the determination of fair value of financial assets and financial liabilities and the supporting assumptions and methodologies. We gain assurance on the overall reasonableness and consistent application of valuation input assumptions, valuation methodologies and compliance with accounting standards for fair value determination through the execution of various processes and controls designed to ensure that our financial assets and financial liabilities are appropriately valued. We monitor fair values received from third parties and those derived internally on an ongoing basis.

In certain situations, we employ independent third-party valuation service providers to gather, analyze, and interpret market information and derive fair values based upon relevant assumptions and methodologies for individual instruments. In situations where our valuation service providers are unable to obtain sufficient market observable information upon which to estimate the fair value for a particular security, fair value is determined either by requesting brokers who are knowledgeable about these securities to provide a single quote or by employing internal valuation models that are widely accepted in the financial services industry. Changing market conditions are incorporated into valuation assumptions and reflected in the fair values, which are validated by calibration and other analytical techniques to available market observable data.

Valuation service providers typically obtain data about market transactions and other key valuation model inputs from multiple sources and, through the use of proprietary algorithms, produce valuation information in the form of a single fair value for individual securities for which a fair value has been requested under the terms of our agreements. For certain equity securities, valuation service providers provide market quotations for completed transactions on the measurement date. For other security types, fair values are derived from the valuation service providers' proprietary valuation models. The inputs used by the valuation service providers include, but are not limited to, market prices from recently completed transactions and transactions of comparable securities, interest rate yield curves, credit spreads, liquidity spread, currency rates, and other market-observable information, as applicable. Credit and liquidity spreads are typically implied from completed transactions and transactions of comparable securities. Valuation service providers also use proprietary discounted cash flow models that are widely accepted in the financial services industry and similar to those used by other market participants to value the same financial instruments. The valuation models take into account, among other things, market observable information as of the measurement date, as described above, as well as the specific attributes of the security being valued including its term, interest rate, credit rating, industry sector, and where applicable, collateral quality and other issue or issuer specific information. Executing valuation models effectively requires seasoned professional judgment and experience. In cases where market transactions or other market observable data is limited, the extent to which judgment is applied varies inversely with the availability of market observable information.

For certain of our financial assets carried at fair value, where our valuation service providers cannot provide fair value determinations, we obtain non-binding price quotes from brokers familiar with the security who, similar to our valuation service providers, may consider transactions or activity in similar securities, as applicable, among other information. The brokers providing price quotes are generally from the brokerage divisions of leading financial institutions with market making, underwriting and distribution

expertise.

The fair value of financial assets and financial liabilities, including privately-placed securities, certain free-standing derivatives and certain derivatives embedded in certain contractholder liabilities, where our valuation service providers or brokers do not provide fair value determinations, is determined using valuation methods and models widely accepted in the financial services industry. Internally developed valuation models, which include inputs that may not be market observable and as such involve some degree of judgment, are considered appropriate for each class of security to which they are applied.

Our internal pricing methods are primarily based on models using discounted cash flow methodologies that determine a single best estimate of fair value for individual financial instruments. In addition, our models use internally assigned credit ratings as inputs (which are generally consistent with any external ratings and those we use to report our holdings by credit rating) and stochastically determined cash flows for certain derivatives embedded in certain contractholder liabilities, both of which are difficult to independently observe and verify. Instrument specific inputs used in our internal fair value determinations include: coupon rate, coupon type, weighted average life, sector of the issuer, call provisions, and the contractual elements of derivatives embedded in certain contractholder liabilities. Market related inputs used in these fair values, which we believe are representative of inputs other market participants would use to determine the fair value of the same instruments include: interest rate yield curves, quoted market prices of comparable securities, credit spreads, estimated liquidity premiums, and other applicable

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market data including lapse and anticipated market return estimates for derivatives embedded in certain contractholder liabilities. Credit spreads are determined using those published by a commonly used industry specialist for comparable public securities. A liquidity premium is also added to certain securities to reflect spreads commonly required for the types of securities being valued and are calibrated based on actual trades or other market data. As a result of the significance of non-market observable inputs, including internally assigned credit ratings and stochastic cash flow estimates as described above, judgment is required in developing these fair values. The fair value of these financial assets and financial liabilities may differ from the amount actually received to sell an asset or the amount paid to transfer a liability in an orderly transaction between market participants at the measurement date. Moreover, the use of different valuation assumptions may have a material effect on the financial assets' and financial liabilities' fair values.

Fair value of our investments comprise an aggregation of numerous, single best estimates for each security in the Consolidated Statements of Financial Position. Because of this detailed approach, there is no single set of assumptions that determine our fair value estimates at a consolidated level. Moreover, management does not compile a range of estimates for items reported at fair value at the consolidated level because we do not believe that a range would provide meaningful information. In the last 10 years, our quarterly net unrealized capital gains and losses have ranged from a \$4.35 billion net unrealized capital gain at June 30, 2003 to a \$6.70 billion net unrealized capital loss at December 31, 2008. The change in net unrealized capital gains and losses by quarter over the 10 year period has averaged \$741 million and has ranged from a \$3.66 billion decrease to a \$1.45 billion increase.

Level 1 and Level 2 measurements represent valuations where all significant inputs are market observable. Level 3 measurements have one or more significant inputs that are not market observable and as a result these fair value determinations have greater potential variability as it relates to their significant inputs. The Level 3 principal components are privately placed securities valued using internal models and broker quoted securities. Additionally, due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market, all asset-backed residential mortgage-backed securities ("ABS RMBS"), auction rate securities ("ARS") backed by student loans, Alt-A residential mortgage-backed securities ("Alt-A"), other collateralized debt obligations ("CDO"), certain asset-backed securities ("ABS") and certain commercial mortgage-backed securities ("CMBS") are categorized as Level 3. In general, the greater the reliance on significant inputs that are not market observable, the greater potential variability of the fair value determinations. For broker quoted securities' fair value determinations, which were all categorized as Level 3, we believe the brokers providing the quotes may consider market observable transactions or activity in similar securities, as applicable, and other information as calibration points. Privately placed securities' fair value determinations, which are based on internal ratings that are not market observable and categorized as Level 3, are calibrated to market observable information in the form of external National Association of Insurance

We believe our most significant exposure to changes in fair value is due to market risk. Our exposure to changes in market conditions is discussed fully in the Market Risk section of the MD&A.

We employ specific control processes to determine the reasonableness of the fair value of our financial assets and financial liabilities. Our processes are designed to ensure that the values received or internally estimated are accurately recorded and that the data inputs and the valuation techniques utilized are appropriate, consistently applied, and that the assumptions are reasonable and consistent with the objective of determining fair value. For example, on a continuing basis, we assess the reasonableness of individual security values received from valuation service providers that exceed certain thresholds as compared to previous values received from those valuation service providers. In addition, we may validate the reasonableness of fair values by comparing information obtained from our valuation service providers to other third party valuation sources for selected financial assets. When fair value determinations are expected to be more variable, we validate them through reviews by members of management who have relevant expertise and who are independent of those charged with executing investment transactions. We do not alter fair values provided by our valuation providers or brokers.

The following table identifies investments as of December 31, 2008 by source of value determination:

INVESTMENTS		

---	(\$ IN	
	MILLIONS)	
FAIR PERCENT		
VALUE TO		
TOTAL	-----	

----- Fair		
value based		
on internal		
sources \$		
8,551	14.3%	
Fair value		
based on		
external		
sources (1)		
37,835	63.3	

-		
- Total		
fixed		
income,		
equity and		
short-term		
securities		
46,386	77.6	
Fair value		
of		
derivatives		
138	0.2	
Mortgage		
loans,		
policy		
loans, bank		
loans and		
limited		
partnership		
and other		
investments,		
valued at		
cost,		
amortized		
cost and the		
equity		
method		
13,248	22.2	

-		
- Total \$		
59,772		

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- - - - -
(1) Includes \$2.58 billion that are valued using broker quotes.

For more detailed information on our accounting policy for the fair value of financial assets and financial liabilities and information on the financial assets and financial liabilities included in the levels promulgated by SFAS No. 157, see Note 2 of the consolidated financial statements.

IMPAIRMENT OF FIXED INCOME AND EQUITY SECURITIES For investments classified as available for sale, the difference between fair value and amortized cost for fixed income securities and cost for equity securities, net of certain other items and deferred income taxes (as disclosed in Note 6), is reported as a component of accumulated other comprehensive income on the Consolidated Statements of Financial Position and is not reflected in the operating results of any period until reclassified to net income upon the consummation of a transaction with an unrelated third party or when the decline in fair value is deemed other than temporary. The assessment of whether the impairment of a security's fair value is other than temporary is performed using a portfolio review as well as a case-by-case review considering a wide range of factors.

There are a number of assumptions and estimates inherent in evaluating impairments and determining if they are other than temporary, including: 1) our ability and intent to hold the investment for a period of time sufficient to allow for an anticipated recovery in value; 2) the expected recoverability of principal and interest; 3) the length of time and extent to which the fair value has been less than amortized cost for fixed income securities or cost for equity securities; 4) the financial condition, near-term and long-term prospects of the issue or issuer, including relevant industry conditions and trends, and implications of rating agency actions and offering prices; and 5) the specific reasons that a security is in a significant unrealized loss position, including market conditions which could affect liquidity. Additionally, once assumptions and estimates are made, any number of changes in facts and circumstances could cause us to subsequently determine that an impairment is other than temporary, including: 1) general economic conditions that are worse than previously forecasted or that have a greater adverse effect on a particular issuer or industry sector than originally estimated; 2) changes in the facts and circumstances related to a particular issue or issuer's ability to meet all of its contractual obligations; and 3) changes in facts and circumstances obtained that causes a change in our ability or intent to hold a security to maturity or until it recovers in value. Examples of situations which may change our ability or intent to hold a security to maturity or recovery include where significant unanticipated new facts and circumstances emerge or existing facts and circumstances increase in significance and are anticipated to adversely impact a security's future valuations more than previously expected, including negative developments that would change the view of long term investors and their intent to continue to hold the investment, subsequent credit deterioration of an issuer or holding, subsequent further deterioration in capital markets (i.e. debt and equity) and of economic conditions, subsequent further deterioration in the financial services and real estate industries, liquidity needs, federal income tax situations involving capital gains and capital loss carrybacks and carryforwards with specific expiration dates, investment risk mitigation actions, and other new facts and circumstances that would cause a change in our previous intent to hold a security to recovery or maturity. Changes in assumptions, facts and circumstances could result in additional charges to earnings in future periods to the extent that losses are realized. The charge to earnings, while potentially significant to net income, would not have a significant effect on shareholder's equity, since our entire portfolio is designated as available-for-sale and carried at fair value and as a result, any related net unrealized loss would already be reflected as a component of accumulated other comprehensive income in shareholder's equity.

The determination of the amount of impairment is an inherently subjective process based on periodic evaluation of the factors described above. Such evaluations and assessments are revised as conditions change and new information becomes available. We update our evaluations regularly and reflect changes in impairments in

results of operations as such evaluations are revised. The use of different methodologies and assumptions as to the determination of the fair value of investments and the timing and amount of impairments may have a material effect on the amounts presented within the consolidated financial statements.

Fixed income securities subject to other-than-temporary impairment write-downs continue to earn investment income when future expected payments are both reasonably estimable and probable, and any discount or premium is recognized using the effective yield method over the expected life of the security; otherwise income recognition is discontinued. For a more detailed discussion of the risks relating to changes in investment values and levels of investment impairment as well as the potential causes of such changes, see Note 6 of the consolidated financial statements and the Investments, Market Risk, and Risk Factors sections of this document.

DEFERRED POLICY ACQUISITION COSTS AMORTIZATION We incur significant costs in connection with acquiring insurance policies and investment contracts. In accordance with GAAP, costs that vary with and are primarily related to acquiring insurance policies and investment contracts are deferred and recorded as an asset on the Consolidated Statements of Financial Position. The amortization methodology for DAC includes significant assumptions and estimates.

DAC related to traditional life insurance is amortized over the premium paying period of the related policies in proportion to the estimated revenues on such business. Significant assumptions relating to estimated premiums, investment returns, which include investment income and realized capital gains and losses, as well as mortality, persistency and expenses to administer the business are established at the time the policy is issued and are generally not revised during the life of the policy. The assumptions for determining DAC amortization are consistent with the assumptions used to calculate the reserve for life-contingent contract benefits. Any deviations from projected business in force resulting from actual policy terminations differing from expected levels and any estimated premium deficiencies may result in a change to the rate of amortization in the period such events occur. Generally, the amortization periods for these policies approximates the estimated lives of the policies. The recovery of DAC is dependent upon the future profitability of this business. We periodically review the adequacy of reserves and recoverability of DAC for these policies on an aggregate basis using actual experience. We aggregate all products accounted for pursuant to Statement of Financial Accounting Standards No. 60, "Accounting and Reporting by Insurance Enterprises" ("SFAS No. 60"), in the analysis. In the event actual experience is significantly adverse compared to the original assumptions, any remaining unamortized DAC balance must be expensed to the extent not recoverable and a premium deficiency reserve may be required if the remaining DAC balance is insufficient to absorb the deficiency. In 2008, for traditional life insurance and immediate annuities with life contingencies, an aggregate premium deficiency of \$336 million pre-tax (\$219 million after-tax) resulted primarily from a study indicating that the annuitants on certain life-contingent contracts are projected to live longer than we anticipated when the contracts were issued and, to a lesser degree, a reduction in the related investment portfolio yield. The deficiency was recorded through a reduction in DAC. In 2007 and 2006, our reviews concluded that no premium deficiency adjustments were necessary, primarily due to projected income from traditional life insurance more than offsetting the projected deficiency in immediate annuities with life contingencies.

DAC related to interest-sensitive life, annuities and other investment contracts is amortized in proportion to the incidence of the total present value of gross profits, which includes both actual historical gross profits ("AGP") and estimated future gross profits ("EGP") expected to be earned over the estimated lives of the contracts. The amortization is net of interest on the prior period DAC balance using rates established at the inception of the contracts. Actual amortization periods generally range from 15-30 years; however, incorporating estimates of customer surrender rates, partial withdrawals and deaths generally results in the majority of the DAC being amortized during the surrender charge period. The cumulative DAC amortization is reestimated and adjusted by a cumulative charge or credit to results of operations when there is a difference between the incidence of actual versus expected gross profits in a reporting period or when there is a change in total EGP.

AGP and EGP consist of the following components: contract charges for the cost of insurance less mortality costs and other benefits (benefit margin); investment income and realized capital gains and losses less interest credited (investment margin); and surrender and other contract charges less maintenance expenses (expense margin). The amount of EGP is principally dependent on assumptions for investment returns, including capital gains and losses on assets supporting contract liabilities, interest crediting rates to contractholders, and the effects of persistency, mortality, expenses, and hedges if applicable, and these assumptions are reasonably likely to have the greatest impact on the amount of DAC amortization. Changes in these assumptions can be offsetting and the Company is unable to reasonably predict their future movements or offsetting impacts over time.

Each reporting period, DAC amortization is recognized in proportion to AGP for that period adjusted for interest on the prior period DAC balance. This amortization process includes an assessment of AGP compared to EGP, the actual

benefit margin to amortization of the DAC balance as of December 31, 2008.

(\$ IN MILLIONS)
DECEMBER 31, 2008
INCREASE/(REDUCTION)
IN DAC -----

Increase in future
investment margins
of 25 basis points \$
169 Decrease in
future investment
margins of 25 basis
points \$ (195)
Decrease in future
life mortality by 1%
\$ 28 Increase in
future life
mortality by 1% \$
(31)

Any potential changes in assumptions discussed above are measured without consideration of correlation among assumptions. Therefore, it would be inappropriate to add them together in an attempt to estimate overall variability in amortization.

For additional discussion see the Risk Factors section of this document and Note 2 and 10 of the consolidated financial statements.

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RESERVE FOR LIFE-CONTINGENT CONTRACT BENEFITS ESTIMATION Benefits for these policies are payable over many years; accordingly, the reserves are calculated as the present value of future expected benefits to be paid, reduced by the present value of future expected net premiums. Long-term actuarial assumptions of future investment yields, mortality, morbidity, policy terminations and expenses are used when establishing the reserve for life-contingent contract benefits payable under insurance policies including traditional life insurance and life-contingent immediate annuities. These assumptions, which for traditional life insurance are applied using the net level premium method, include provisions for adverse deviation and generally vary by characteristics such as type of coverage, year of issue and policy duration. Future investment yield assumptions are determined based upon prevailing investment yields as well as estimated reinvestment yields. Mortality, morbidity and policy termination assumptions are based on our experience and industry experience. Expense assumptions include the estimated effects of inflation and expenses to be incurred beyond the premium-paying period. These assumptions are established at the time the policy is issued, are consistent with assumptions for determining DAC amortization for these policies, and are generally not changed during the policy coverage period. However, if actual experience emerges in a manner that is significantly adverse relative to the original assumptions, adjustments to DAC or reserves may be required resulting in a charge to earnings which could have a material adverse effect on our operating results and financial condition. We periodically review the adequacy of these reserves and recoverability of DAC for these policies on an aggregate basis using actual experience. In the event that actual experience is significantly adverse compared to the original assumptions, any remaining unamortized DAC balance must be expensed to the extent not recoverable and the establishment of a premium deficiency reserve may be required. The effects of changes in reserve estimates are reported in the results of operations in the period in which the changes are determined. In 2008, for traditional life insurance and immediate annuities with life contingencies, an aggregate premium deficiency of \$336 million pre-tax (\$219 million after-tax) resulted primarily from a study indicating that the annuitants on certain life-contingent contracts are projected to live longer than we anticipated when the contracts were issued and, to a lesser degree, a reduction in the related investment portfolio yield. The deficiency was recorded through a reduction in DAC. In 2007 and 2006, our reviews concluded that no premium deficiency adjustments were necessary, primarily due to projected income from traditional life insurance more than offsetting the projected deficiency in immediate annuities with life contingencies. We will continue to monitor the experience of our traditional life insurance and immediate annuities. Further significant changes in mortality experience or the portfolio yield could result in additional charges in future periods. We anticipate that mortality, investment and reinvestment yields, and policy terminations are the factors that would be most likely to require adjustment to these reserves or related DAC.

For further discussion of these policies, see Note 8 of the consolidated financial statements and the Risk Factors section of this document.

2008 HIGHLIGHTS

- Net loss was \$1.69 billion in 2008 compared to net income of \$412 million in 2007.
- Net realized capital losses totaled \$3.05 billion in 2008 compared to \$197 million in 2007.
- During 2008, we recorded \$399 million in accelerated DAC and deferred sales inducement costs ("DSI") amortization related to deferred annuities and interest-sensitive life insurance due to changes in assumptions (which resulted in changes to total EGP). Additional amortization of DAC totaling \$336 million was recorded in connection with a premium deficiency assessment for traditional life insurance and immediate annuities with life contingencies primarily due to revised annuity mortality assumptions.
- Contractholder fund deposits totaled \$9.29 billion for 2008 compared to \$7.96 billion for 2007.
- Investments as of December 31, 2008 decreased 17.5% to \$59.77 billion from \$72.41 billion as of December 31, 2007 and net investment income decreased 11.5% to \$3.72 billion in 2008 from \$4.21 billion in 2007.
- Continued focus on improving returns and reducing our concentration in spread based products, primarily fixed annuities and institutional markets products.
- Launched an initiative that will result in lower operating expenses in 2009 and 2010, and targeting annual savings of \$90 million beginning in 2011.

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OPERATIONS

OVERVIEW AND STRATEGY We are a major provider of life insurance, retirement and investment products to individual and institutional customers. We serve these customers through Allstate exclusive agencies and non-proprietary distribution channels. Our strategic vision is to reinvent protection and retirement for the consumer.

To achieve our vision and reach our financial goals, our primary objectives are to deepen financial services relationships with Allstate customers and restore profitability through operational excellence and portfolio optimization. Sales in non-proprietary channels will be increasingly tactical as we assess market opportunities. In addition to focusing on higher return markets, products, and distribution channels, we will continue to emphasize capital efficiency and enterprise risk and return management strategies and actions.

Our strategy provides a platform to profitably grow our business. Based upon Allstate's strong financial position and brand, our customers seek assistance in meeting their protection and retirement needs through trusted relationships. We have unique access to potential customers through cross-sell opportunities within the Allstate exclusive agencies. Our investment expertise, strong operating platform and solid relationships with distribution partners provide a foundation to deliver value to our customers.

We plan to offer a more focused suite of products designed for middle market consumers to help everyday Americans meet their financial protection needs and help them better prepare for retirement. Our products include fixed annuities, including deferred, immediate and indexed; interest-sensitive, traditional and variable life insurance; and funding agreements backing medium-term notes. Our products are sold through a wide range of distribution channels including Allstate exclusive agencies, which include exclusive financial specialists, independent agents (including master brokerage agencies), financial service firms such as banks and broker-dealers, and specialized structured settlement brokers. Our institutional product line consists primarily of funding agreements sold to unaffiliated trusts that use them to back medium-term notes issued to institutional and individual investors.

Summarized financial data for the years ended December 31 is presented in the following table.

(\$ IN MILLIONS)	
2008	2007
2006	-----
---	-----
--	-----
- REVENUES	
Premiums (1)	
\$ 585	\$ 502
576	Contract
911	charges (1)
942	1,009
1,009	Net

investment	
income	3,720
4,205	4,057
Realized	
capital gains	
and losses	
(3,052)	(197)
(79)	-----
---	-----
- Total	
revenues	
2,164	5,452
5,563	COSTS
AND EXPENSES	
Contract	
benefits	
(1,397)	
(1,364)	
(1,372)	
Interest	
credited to	
contractholder	
funds (2,356)	
(2,628)	
(2,543)	
Amortization	
of DAC (643)	
(518)	(538)
Operating	
costs and	
expenses	
(399)	(338)
(374)	
Restructuring	
and related	
charges (1)	
(2)	(24) ----
-----	-----
-----	-----
-----	Total
-----	costs and
-----	expenses
-----	(4,796)
-----	(4,850)
(4,851)	Loss
on	
disposition	
of operations	
(4)	(10) (88)
Income tax	
benefit	
(expense) 946	
(180)	(196) -
-----	-----
-----	-----
-----	Net
(loss) income	
\$ (1,690)	\$
412	\$ 428
=====	
=====	
=====	
Investments	
at December	
31	\$ 59,772 \$
72,414	\$
74,160	
=====	
=====	
=====	

(1) Beginning in 2008, certain ceded reinsurance premiums previously included as a component of traditional life insurance premiums were reclassified prospectively to be reported as a component of interest-sensitive life insurance contract charges. In 2007 and 2006, these ceded reinsurance premiums were \$90 million and \$53 million, respectively.

Effective June 1, 2006, the Company disposed of substantially all of its variable annuity business through reinsurance with Prudential Financial Inc. ("Prudential"). The following table presents the results of operations attributable to our reinsured variable annuity business for the period of 2006 prior to the disposition.

(\$ IN
MILLIONS)
2006 -----
-- Contract
charges \$ 136
Net
investment
income 17
Realized
capital gains
and losses
(8) -----
- Total
revenues 145
Contract
benefits (13)
Interest
credited to
contractholder
funds (24)
Amortization
of deferred
policy
acquisition
costs (44)
Operating
costs and
expenses (43)

Total costs
and expenses
(124) Loss on
disposition
of operations
(89) -----
-- Income
from
operations
before income
tax expense
(1) \$ (68)
=====

-
- (1) For 2006, income from operations before income tax expense attributable to the variable annuity business reinsured to Prudential included investment spread and benefit spread of \$(7) million and \$13 million, respectively.

NET LOSS in 2008 was \$1.69 billion compared to net income of \$412 million and \$428 million in 2007 and 2006, respectively. The change in 2008 was primarily the result of the recognition of higher net realized capital losses in the current year compared to the prior year and, to a lesser extent, DAC and DSI amortization acceleration for changes in assumptions and additional amortization of DAC that was recorded in connection with a premium deficiency assessment for traditional life insurance and immediate annuities with life contingencies due to revised annuity mortality assumptions. Net income in 2007 was comparable to 2006 as lower losses associated with dispositions of operations were almost entirely offset by a decline in total revenues.

ANALYSIS OF REVENUES Total revenues decreased 60.3% or \$3.29 billion in 2008 compared to 2007, due to a \$2.86 billion increase in net realized capital losses and a \$485 million decrease in net investment income. Total revenues decreased 2.0% or \$111 million in 2007 compared to 2006, due to higher net realized capital losses and lower premiums and contract charges, partially offset by higher net investment income.

PREMIUMS represent revenues generated from traditional life insurance, immediate annuities with life contingencies, and accident, health and other insurance products that have significant mortality or morbidity risk.

CONTRACT CHARGES are revenues generated from interest-sensitive and variable life insurance, fixed annuities and variable annuities for which deposits are classified as contractholder funds or separate accounts liabilities. Contract charges are assessed against the contractholder account values for maintenance, administration, cost of insurance and surrender prior to contractually specified dates. As a result, changes in contractholder funds are considered in the evaluation of growth and as indicators of future levels of revenues. Subsequent to the close of our reinsurance transaction with Prudential effective June 1, 2006, variable annuity contract charges on the business subject to the transaction are fully reinsured to Prudential and presented net of reinsurance on the Consolidated Statements of Operations and Comprehensive Income (see Note 3 to the consolidated financial statements).

The following table summarizes premiums and contract charges by product.

(\$ IN MILLIONS)	
2008	2007
2006	-----
-----	-----
- PREMIUMS	
Traditional life insurance	
(1) \$ 368	\$ 260
\$ 260	\$ 257
Immediate annuities with life contingencies	
132	204
278	
Accident, health and other	
85	38
41	-----
-----	-----
TOTAL PREMIUMS	
585	502
576	
CONTRACT CHARGES	
Interest-sensitive life insurance	
(1) 855	862
797	
Fixed annuities	
55	79
73	
Variable annuities	
1	139
-----	-----
-----	-----
-- TOTAL CONTRACT CHARGES (2)	
911	942
1,009	-----
-----	-----
-- TOTAL PREMIUMS AND CONTRACT CHARGES \$	
1,496	\$ 1,444
\$ 1,444	\$ 1,585
=====	=====
=====	=====
=====	-----

(1) Beginning in 2008, certain ceded reinsurance premiums previously

included as a component of traditional life insurance premiums were reclassified prospectively to be reported as a component of interest-sensitive life insurance contract charges. In 2007 and 2006, these ceded reinsurance premiums were \$90 million and \$53 million, respectively.

- (2) Contract charges primarily reflect non-cash charges to contractholder account balances. Total contract charges for 2008, 2007 and 2006 include contract charges related to the cost of insurance of \$572 million, \$617 million and \$600 million, respectively.

Total premiums increased 16.5% in 2008 compared to 2007, due to the prospective reporting reclassification for certain ceded reinsurance premiums. Excluding the impact of this reporting reclassification, total premiums decreased 1.2% in 2008 compared to 2007 as higher sales of traditional life insurance and increased accident and health insurance premiums assumed from American Heritage Life Insurance Company, an unconsolidated affiliate, were more than offset by lower sales of immediate annuities with life contingencies due to highly competitive market conditions and our continued focus on returns.

Total premiums decreased 12.8% in 2007 compared to 2006 as higher sales of traditional life insurance products were more than offset by a decline in sales of life contingent immediate annuities due to market competitiveness.

Total premiums in the three years ended December 31, 2008, adjusted for the reporting reclassification of certain ceded reinsurance premiums, averaged \$602 million.

Total contract charges decreased 3.3% in 2008 compared to 2007 due to the prospective reporting reclassification of certain ceded reinsurance premiums. Excluding the impact of this reclassification, total contract charges increased 6.9% in 2008 due to higher contract charges on interest-sensitive life insurance policies resulting from increased contract charge rates and growth in business in force, partially offset by decreased contract charges on fixed annuities resulting primarily from lower contract surrenders.

Contract charges decreased 6.6% in 2007 compared to 2006 due to the disposal of substantially all of our variable annuity business through reinsurance effective June 1, 2006. Excluding contract charges on variable annuities, substantially all of which are reinsured to Prudential effective June 1, 2006, contract charges increased 8.2% in 2007 compared to 2006. The increase reflects growth in interest-sensitive life insurance policies in force, higher maintenance charge rates on interest-sensitive life products and, to a lesser extent, higher contract charges on fixed annuities. The increase in contract charges on fixed annuities was mostly attributable to higher contract surrenders.

CONTRACTHOLDER FUNDS represent interest-bearing liabilities arising from the sale of individual and institutional products, such as interest-sensitive life insurance, fixed annuities and funding agreements. The balance of contractholder funds is equal to the cumulative deposits received and interest credited to the contractholder less cumulative contract maturities, benefits, surrenders, withdrawals and contract charges for mortality or administrative expenses.

The following table shows the changes in contractholder funds.

(\$ IN MILLIONS)	
2008	2007
2006	-----
-----	-----
-----	-----
----	----
CONTRACTHOLDER FUNDS,	
BEGINNING BALANCE \$	
60,464	\$
60,565	\$
58,190	
DEPOSITS	
Fixed annuities	
3,801	3,635
6,006	
Institutional products (funding	

agreements)		
4,158	3,000	
2,100		
Interest-sensitive life insurance		
1,325	1,324	
1,336		
Variable annuity and life deposits allocated to fixed accounts		
2	1	
99	-----	
--	-----	
--	-----	
-- Total deposits		
9,286	7,960	
9,541		
INTEREST CREDITED		
2,350	2,635	
2,600		
MATURITIES, BENEFITS, WITHDRAWALS AND OTHER ADJUSTMENTS		
Maturities and retirements of institutional products		
(8,599)		
(3,165)		
(2,726)		
Benefits		
(1,701)		
(1,656)		
(1,500)		
Surrenders and partial withdrawals		
(4,329)		
(4,928)		
(4,627)		
Contract charges	(819)	
(751)	(697)	
Net transfers from (to) separate accounts		
19	(145)	
34	38	Fair value hedge adjustments for institutional products
(56)		
34	38	Other adjustments
(1)	165	(243)
(109)	-----	
-----	-----	
-----	-----	
----- Total maturities, benefits, withdrawals and other adjustments		
(15,320)		
(10,696)		
(9,766)	-----	
-----	-----	
-----	-----	
-----	-----	

CONTRACTHOLDER
 FUNDS, ENDING
 BALANCE \$
 56,780 \$
 60,464 \$
 60,565
 =====
 =====
 =====

(1) The table above illustrates the changes in contractholder funds, which are presented gross of reinsurance recoverables on the Consolidated Statements of Financial Position. The table above is intended to supplement our discussion and analysis of revenues, which are presented net of reinsurance on the Consolidated Statements of Operations and Comprehensive Income. As a result, the net change in contractholder funds associated with products reinsured to third parties is reflected as a component of the other adjustments line. This includes, but is not limited to, the net change in contractholder funds associated with the reinsured variable annuity business subsequent to the effective date of our reinsurance agreements with Prudential (see Note 3 to the consolidated financial statements).

Contractholder funds decreased 6.1% and 0.2% in 2008 and 2007, respectively, and increased 4.1% in 2006. Average contractholder funds decreased 3.1% in 2008 compared to 2007, and increased 1.9% in 2007 compared to 2006.

Contractholder deposits increased 16.7% in 2008 compared to 2007 due primarily to higher deposits on institutional products, and to a lesser extent, higher deposits on fixed annuities. Sales of our institutional products vary from period to period based on management's assessment of market conditions, investor demand and operational priorities. Deposits on fixed annuities increased 4.6% in 2008 compared to 2007 due primarily to increased consumer demand as the attractiveness of fixed annuities relative to competing products improved, partially offset by pricing decisions aimed to increase new business returns.

Contractholder deposits decreased 16.6% in 2007 compared to 2006. The decline was primarily due to lower deposits on fixed annuities partially offset by higher deposits on institutional products. The decline of 39.5% in fixed annuity deposits in 2007 compared to 2006 was due to our strategy to raise new business returns for these products combined with lower industry-wide fixed annuity sales. Deposits on institutional products increased 42.9% in 2007 compared to 2006.

Contractholder deposits on fixed annuities have varied over the past several years based on factors such as the attractiveness of fixed annuities to consumers relative to other investment alternatives, the competitiveness of our crediting rates, and our target returns on newly issued fixed annuity contracts. The level of fixed annuity deposits in 2008 and 2007 was also influenced by our strategy to raise new business returns, which we continue to pursue. Beginning in 2009, we intend to reduce our concentration of spread based business, including fixed annuities.

Maturities and retirements of institutional products increased \$5.43 billion in 2008 compared to 2007. During 2008, we retired \$5.36 billion of extendible institutional market obligations for which investors had elected to non-extend their maturity date through a combination of maturities, calls, and acquisitions in the secondary market. All of our outstanding extendible institutional market contracts, which totaled \$1.45 billion as of December 31, 2008, have non-extended. We have called \$1.21 billion of these contracts and we will retire them in March 2009; the remainder will become due by July 31, 2009. We have accumulated, and expect to maintain, short-term and other maturing investments to fund the retirement of these obligations. We will assess market conditions and may take actions in the secondary market to retire additional institutional market obligations prior to their stated maturity.

Surrenders and partial withdrawals decreased 12.2% to \$4.33 billion in 2008 from \$4.93 billion in 2007 due to lower surrenders and partial withdrawals on market value adjusted annuities and traditional fixed annuities, partially offset by higher surrenders and partial withdrawals on interest-sensitive life insurance products. The surrender and

partial withdrawal rate on deferred fixed annuities and interest-sensitive life insurance products, based on the beginning of period contractholder funds, was 10.3% in 2008 compared to 11.6% in 2007.

Surrenders and partial withdrawals increased 6.5% in 2007 compared to 2006 due primarily to an 11.3% increase in surrenders and partial withdrawals on fixed annuities. This increase was partially offset by lower surrenders and partial withdrawals on interest-sensitive life insurance policies and the classification of the net change in variable annuity contractholder funds as "other adjustments" subsequent to the effective date of our reinsurance agreements with Prudential. The surrenders and partial withdrawals line in the table above, for 2006 includes \$120 million related to the reinsured variable annuity business. The surrender and partial withdrawal rate on deferred fixed annuities and interest-sensitive life insurance products, based on the beginning of period contractholder funds, was 11.6% in 2007 compared to 11.3% in 2006.

NET INVESTMENT INCOME decreased 11.5% in 2008 compared to 2007 and increased 3.6% in 2007 compared to 2006. The decline in 2008 was primarily due to lower investment yields on floating rate securities, increased short-term investment balances reflecting liquidity management activities, lower average investment balances and lower income from limited partnership interests. The increase in 2007 was primarily due to higher average portfolio balances, increased portfolio yields and higher income from limited partnership interests.

REALIZED CAPITAL GAINS AND LOSSES reflected net losses of \$3.05 billion, \$197 million and \$79 million in 2008, 2007 and 2006, respectively. For further discussion of realized capital gains and losses, see the Investments section of MD&A.

ANALYSIS OF COSTS AND EXPENSES Total costs and expenses decreased 1.1% or \$54 million in 2008 compared to 2007 due to lower interest credited to contractholder funds, partially offset by higher amortization of DAC, contract benefits and operating costs and expenses. Total costs and expenses in 2007 were consistent with 2006 as increased interest credited to contractholder funds was offset by lower amortization of DAC, operating costs and expenses, and restructuring and related charges.

CONTRACT BENEFITS increased 2.4% or \$33 million in 2008 compared to 2007 due primarily to higher contract benefits on life insurance products, partially offset by lower contract benefits on annuities. The increase in contract benefits on life insurance products was primarily due to unfavorable mortality experience, partially offset by the recognition in the prior year period of litigation related costs in the form of additional policy benefits. The decline in contract benefits on annuities was due to the impact of lower sales of immediate annuities with life contingencies, partially offset by unfavorable mortality experience.

Contract benefits decreased 0.6% or \$8 million in 2007 compared to 2006 due to lower contract benefits on annuities, partially offset by higher contract benefits on life insurance products. The decline in contract benefits on annuities was mostly attributable to favorable mortality experience and lower sales of immediate annuities with life contingencies and the absence in 2007 of contract benefits on the reinsured variable annuity business, partially offset by an increase in the implied interest on immediate annuities with life contingencies.

We analyze our mortality and morbidity results using the difference between premiums and contract charges earned for the cost of insurance and contract benefits excluding the portion related to the implied interest on immediate annuities with life contingencies ("benefit spread"). This implied interest totaled \$552 million, \$547 million and \$539 million in 2008, 2007 and 2006, respectively. The benefit spread by product group is disclosed in the following table.

(\$ IN MILLIONS)	
2008	2007
2006	-----

Life insurance	
\$ 374	\$ 337
\$ 386	
Annuities	
(62)	(35)
(43)	-----

Total benefit spread	
\$ 312	\$ 302

=====
 =====
 =====

INTEREST CREDITED TO CONTRACTHOLDER FUNDS, which represents non-cash charges for interest accrued on interest-sensitive life and investment contracts, decreased 10.4% or \$272 million in 2008 compared to 2007 and increased 3.3% or \$85 million in 2007 compared to 2006. The decrease in 2008 compared to 2007 was due primarily to a decline in average contractholder funds, decreased weighted average interest crediting rates on institutional products resulting from a decline in market interest rates on floating rate obligations, and a favorable change in amortization of DSI relating to realized capital gains and losses, partially offset by the acceleration of amortization of DSI due to changes in assumptions. The acceleration of amortization of DSI due to changes in assumptions increased interest

credited to contractholder funds by \$70 million in 2008 compared to amortization deceleration which decreased interest credited to contractholder funds by \$5 million in 2007.

The increase in interest credited to contractholder funds in 2007 compared to 2006 was due primarily to growth in average contractholder funds and, to a lesser extent, higher weighted average interest crediting rates on institutional products, which are detailed in the table of investment yields, crediting rates and investment spreads by product below. The increase was partially offset by the impact of the reinsured variable annuity business. Excluding the impact of the reinsured variable annuity business, interest credited to contractholder funds increased 4.3% in 2007 compared to 2006.

In order to analyze the impact of net investment income and interest credited to contractholders on net income, we monitor the difference between net investment income and the sum of interest credited to contractholder funds and the implied interest on immediate annuities with life contingencies, which is included as a component of contract benefits on the Consolidated Statements of Operations and Comprehensive Income ("investment spread").

The investment spread by product group is shown in the following table.

(\$ IN MILLIONS)	
2008	2007
2006	-----
---	-----
---	-----
- Annuities	
\$ 388	\$ 504
\$ 480	Life
insurance	50
55	49
Institutional	
products	71
87	88
Net	
investment	
income on	
investments	
supporting	
capital	303
384	358
----	----
-----	-----
----	Total
investment	
spread	\$ 812
\$ 1,030	\$
975	
=====	
=====	
=====	

To further analyze investment spreads, the following table summarizes the weighted average investment yield on assets supporting product liabilities and capital, interest crediting rates and investment spreads for 2008, 2007 and 2006.

AVERAGE
WEIGHTED
AVERAGE
WEIGHTED
AVERAGE
INVESTMENT
YIELD
INTEREST
CREDITING
RATE
INVESTMENT
SPREADS ----

----- 2008
2007 2006
2008 2007
2006 2008
2007 2006 --
-- -----

Interest-
sensitive
life
insurance
6.0% 6.2%
6.2% 4.6%
4.6% 4.7%
1.4% 1.6%
1.5%
Deferred
fixed
annuities
5.6 5.8 5.7
3.8 3.7 3.7
1.8 2.1 2.0
Immediate
fixed
annuities
with and
without life
contingencies
6.8 7.1 7.2
6.5 6.5 6.6
0.3 0.6 0.6
Institutional
products 4.2
6.1 6.0 3.5
5.2 5.0 0.7
0.9 1.0
Investments
supporting
capital,
traditional
life and
other
products 5.3
6.3 6.2 N/A
N/A N/A N/A
N/A N/A

The following table summarizes our product liabilities as of December 31 and indicates the account value of those contracts and policies in which an investment spread is generated.

(\$ IN
MILLIONS)
2008 2007
2006 -----

Immediate
fixed
annuities
with life
contingencies

changes in
 assumptions
 and premium
 deficiency
 (1) \$ (493) \$
 (547) \$ (586)
 Accretion
 relating to
 realized
 capital gains
 and losses
 (2) 515 17 50
 Amortization
 (acceleration)
 deceleration
 for changes
 in
 assumptions
 ("DAC
 unlocking")
 (329) 12 (2)
 Amortization
 charge
 relating to
 premium
 deficiency
 (336) -- -- -

 ----- Total
 amortization
 of DAC (3)
 (4) \$ (643) \$
 (518) \$ (538)
 =====
 =====
 =====

-
- (1) Amortization of DAC before accretion relating to realized capital gains and losses and changes in assumptions for 2006 includes \$(72) million relating to the reinsured variable annuity business.
 - (2) Amortization relating to realized capital gains and losses for 2006 includes \$28 million relating to the reinsured variable annuity business.
 - (3) Total amortization of DAC for 2006 includes \$44 million relating to the reinsured variable annuity business.
 - (4) Amortization of DAC reflects a non-cash charge to the Consolidated Statements of Operations and Comprehensive Income.

The increase of \$125 million in 2008 was due primarily to amortization acceleration relating to changes in assumptions and additional amortization recorded in connection with a premium deficiency assessment for traditional life insurance and immediate annuities with life contingencies, partially offset by higher accretion of DAC relating to net realized capital losses.

The impact of realized capital gains and losses on amortization of DAC is dependent upon the relationship between the assets that give rise to the gain or loss and the product liability supported by the assets. Fluctuations result from changes in the impact of realized capital gains and losses on actual and expected gross profits.

In 2008, DAC amortization acceleration for changes in assumptions, recorded in connection with comprehensive reviews of the DAC balances and assumptions for interest-sensitive life insurance, annuities and other investment contracts, resulted in an increase to amortization of DAC of \$329 million. The evaluations covered assumptions for investment returns, including capital gains and losses, interest crediting rates to policyholders, the effect of any hedges, persistency, mortality and expenses in all product lines. The principle assumption impacting the amortization acceleration in 2008 was the level of realized capital losses impacting actual gross profits in 2008 and the impact of realized capital losses on EGP in 2009. During the fourth quarter of 2008, our assumptions for EGP were impacted by a view of further anticipated impairments in our investment portfolio. In 2007, DAC amortization deceleration for changes in assumptions (credit to income) was \$12 million.

During 2008, indicators emerged that suggested a study of mortality experience for our immediate annuities with life contingences was warranted. At the same time, the underlying profitability of the traditional life business

\$ 402 \$ 3,905
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

- - - - -
- (1) The DAC balance increased \$32 million during 2008 as a result of a reinsurance transaction. Effective January 1, 2008, the Company's coinsurance reinsurance agreement with its unconsolidated affiliate American Heritage Life Insurance Company ("AHL"), which went into effect in 2004, was amended to include the assumption by the Company of certain accident and health insurance policies.
 - (2) Total acquisition costs deferred in 2008 and 2007 include commissions paid totaling \$464 million and \$435 million, respectively.
 - (3) Amortization before adjustments reflects total DAC amortization before accretion relating to realized capital gains and losses, and amortization (acceleration) deceleration (charged) credited to income.
 - (4) Included as a component of amortization of DAC on the Consolidated Statements of Operations and Comprehensive Income.
 - (5) The \$(336) million in the traditional life and other line was recorded in connection with a premium deficiency assessment for traditional life insurance and immediate annuities with life contingencies and was primarily due to revised annuity mortality assumptions.
 - (6) The effect of unrealized capital gains and losses represents the amount by which the amortization of DAC would increase or decrease if the unrealized capital gains and losses in the respective product portfolios were realized. Recapitalization of DAC is limited to the originally deferred policy acquisition costs plus interest.
 - (7) The adoption of Statement of Position 05-1, "Accounting by Insurance Enterprises for Deferred Acquisition Costs in Connection with Modifications or Exchanges of Insurance Contracts" ("SOP 05-1"), resulted in an adjustment to unamortized DAC related to the impact on future estimated gross profits from the changes in accounting for certain costs associated with contract continuations that no longer qualify for deferral under SOP 05-1. The adjustment was recorded as a \$7 million reduction of retained income at January 1, 2007 and a reduction of the DAC balance of \$11 million, pre-tax.

OPERATING COSTS AND EXPENSES increased 18.1% in 2008 compared to 2007 and decreased 9.6% in 2007 compared to 2006. The following table summarizes operating costs and expenses.

(\$ IN MILLIONS)	
2008	2007
2006	-----
-	-----
-----	-
-----	-----
Non-deferrable acquisition costs	\$ 82
Other operating costs and expenses	\$ 97
	\$ 118
	317
	241
	256

	-

Total operating costs and expenses	\$ 399
	\$ 374
	=====
	=====
Restructuring and related charges	\$ 1
	\$ 2
	\$ 24
	=====

=====
=====

Non-deferrable acquisition costs decreased 15.5% or \$15 million in 2008 compared to 2007 primarily due to lower non-deferrable commissions. Other operating costs and expenses increased 31.5% or \$76 million in 2008 compared to 2007 due primarily to increased spending on consumer research, product development, marketing and technology related to the effort to reinvent protection and retirement for consumers as well as increases in the net cost of benefits due to unfavorable investment results. In addition, the prior years benefitted to a greater degree from a servicing fee paid by Prudential for our servicing of the variable annuity business that we ceded to them during a transition period beginning in 2006 which ended in May 2008.

Non-deferrable acquisition costs and other operating costs and expenses declined in 2007 compared to 2006 due to expenses in 2006 related to the reinsured variable annuity business. Non-deferrable acquisition costs and other operating costs and expenses for 2006 included \$19 million and \$24 million, respectively, related to the reinsured variable annuity business for the period of 2006 prior to the effective date of the reinsurance agreement. Excluding expenses associated with the impact of the reinsured variable annuity business in the period of 2006 prior to the effective date of the reinsurance agreement, non-deferrable acquisition expenses decreased 2.0% in 2007 compared to 2006 due to lower premium taxes and decreased non-deferrable commissions on certain immediate annuities and other operating costs and expenses increased 3.9% due to higher investment in technology.

Restructuring and related charges for 2006 reflect costs related to the Voluntary Termination Offer ("VTO"). The VTO was offered to most employees located at the Company's headquarters and was completed during 2006.

LOSS ON DISPOSITION OF OPERATIONS for 2008, 2007 and 2006 totaled \$4 million, \$10 million and \$88 million, respectively. In both 2008 and 2007, the net loss was primarily comprised of losses associated with the previously anticipated disposition of our direct response long-term care business, partially offset by amortization of the deferred reinsurance gain associated with our reinsured variable annuity business. The net loss in 2006 was almost entirely attributable to the reinsured variable annuity business.

INCOME TAX BENEFIT of \$946 million in 2008 compared to income tax expense of \$180 million in 2007. The change reflects the shift from net pre-tax income in 2007 to a net pre-tax loss in 2008. Income tax expense decreased by 8.2% or \$16 million in 2007 compared to 2006 due to lower income from operations before income tax expense and an energy tax credit that reduced income tax expense.

The Company's effective tax rate is impacted by tax favored investment income such as dividends qualifying for the dividends received deduction ("DRD"). In 2007, the Internal Revenue Service ("IRS") announced its intention to issue regulations dealing with certain computational aspects of the DRD related to separate account assets ("separate accounts DRD"). The ultimate timing and substance of any such regulations are unknown at this time, but may result in the elimination of some or all of the separate accounts DRD tax benefit reflected as a component of the Company's income tax expense. The Company recognized a tax benefit from the separate accounts DRD of \$15 million, \$16 million and \$21 million in 2008, 2007 and 2006, respectively.

REINSURANCE CEDED We enter into reinsurance agreements with unaffiliated reinsurers to limit our risk of mortality and morbidity losses. In addition, the Company has used reinsurance to effect the acquisition or disposition of certain blocks of business. We retain primary liability as a direct insurer for all risks ceded to reinsurers.

As of December 31, 2008 and 2007, 47% and 49%, respectively, of our face amount of life insurance in force was reinsured. As of December 31, 2008 and 2007, for certain term life insurance policies, we ceded up to 90% of the mortality risk depending on the year of policy issuance. Additionally, we ceded substantially all of the risk associated with our variable annuity business and we cede 100% of the morbidity risk on substantially all of our long-term care contracts. Beginning in July 2007, for new life insurance contracts, we ceded mortality risk associated with coverage in excess of \$3 million per life for contracts issued to individuals age 70 and over, and we ceded the mortality risk associated with coverage in excess of \$5 million per life for most other contracts. Also, beginning in July 2007, for certain large contracts that meet specific criteria, our retention limit was increased to \$10 million per life. In the period prior to July 2007, but subsequent to August 1998, we ceded the mortality risk

associated with coverage in excess of \$2 million per life, except in 2006 for certain instances when specific criteria were met, we ceded the mortality risk associated with coverage in excess of \$5 million per life. For business sold prior to October 1998, we ceded mortality risk in excess of specific amounts up to \$1 million per individual life.

Amounts recoverable from reinsurers by type of policy or contract at December 31, are summarized in the following table.

REINSURANCE RECOVERABLE ON PAID AND UNPAID BENEFITS (\$ IN MILLIONS) - ----- ----- ---- 2008 2007 ----- ----- ----- Annuities (1) \$ 1,734 \$ 1,423 Life insurance 1,465 1,365 Long-term care 630 526 Other 94 96 ----- ----- ----- Total \$ 3,923 \$ 3,410 =====

(1) Reinsurance recoverables as of December 31, 2008 and 2007 include \$1.57 billion and \$1.26 billion, respectively, for general account reserves related to reinsured variable annuities.

The estimation of reinsurance recoverables is impacted by the uncertainties involved in the establishment of reserves.

Our reinsurance recoverables, summarized by reinsurer as of December 31, are shown in the following table.

S&P FINANCIAL REINSURANCE RECOVERABLE STRENGTH ON PAID AND (\$ IN MILLIONS) RATING (3) UNPAID BENEFITS -- ----- ----- - 2008 2007 ----- ----- Prudential Insurance Company of America AA- \$ 1,569 \$ 1,261 Employers Reassurance Corporation A+ 644 541 Transamerica

Life Group
AA 341 288
RGA
Reinsurance
Company AA-
340 325
Swiss Re
Life and
Health
America,
Inc. A+ 191
172 Paul
Revere Life
Insurance
Company A-
151 147
Scottish Re
Group (1)
CCC 135 110
Munich
American
Reassurance
AA- 113 103
Security
Life of
Denver AA
86 86
Manulife
Insurance
Company AA+
74 78
Triton
Insurance
Company NR
66 73
Lincoln
National
Life
Insurance
AA- 63 63
American
Health &
Life
Insurance
Co. NR 53
57 Other
(2) 97 106

Total \$
3,923 \$
3,410
=====

-
- (1) The reinsurance recoverable on paid and unpaid benefits related to the Scottish Re Group of \$135 million as of December 31, 2008 is comprised of \$73 million related to Scottish Re Life Corporation and \$62 million related to Scottish Re (U.S.), Inc.
 - (2) As of December 31, 2008 and 2007, the other category includes \$81 million and \$69 million, respectively, of recoverables due from reinsurers with an investment grade credit rating from Standard & Poor's ("S&P").
 - (3) Rating as of March 6, 2009.

During 2008, the financial strength rating of the Scottish Re Group was downgraded by S&P to CCC+ from BB+ as of December 31, 2007 due to the deterioration of the Scottish Re Group's financial position and liquidity. The Scottish Re Group's financial strength rating was further downgraded by S&P in January 2009 to CCC. Although a significant impact has not been observed, the unprecedented deterioration in the global financial markets in 2008 could impact the financial condition of reinsurers in a variety of ways, including the decline in value of assets held as capital resources or to meet technical provisions, increases in risk-based economic or regulatory capital requirements and shortage of available capital in the event that recapitalization is required following a major claim. We continuously monitor the creditworthiness of reinsurers in order to determine our risk of recoverability on an individual and aggregate basis, and a provision for uncollectible reinsurance is recorded if needed. No amounts have been deemed unrecoverable in the three-years ended

ALIC's insurance subsidiaries are domiciled in Illinois, New York, South Carolina and Nebraska. Except for those domiciled in New York and South Carolina, ALIC has 100% intercompany reinsurance agreements in place with its other domestic insurance subsidiaries. With the exception of Allstate Life Insurance Company of New York, which retains substantially all of its business up to its per life limit, and ALIC Reinsurance Company, which is a special purpose financial captive, only invested assets supporting capital and relating to Separate Accounts remain in ALIC's other subsidiaries. All significant intercompany transactions have been eliminated in consolidation.

OUTLOOK

- - We will continue to focus on improving returns and reducing our concentration in spread based products, primarily fixed annuities and institutional markets products, resulting in lower premiums and deposits and reductions in net contractholder obligations.
- - We plan to improve efficiency and narrow the focus of product offerings to better serve the needs of everyday Americans. We are targeting savings at 20% of certain operating expenses, excluding acquisition costs, and expect to yield estimated annual savings of \$90 million beginning in 2011. We anticipate a reduction of approximately 1,000 workforce positions, through a combination of attrition and position elimination over the next two years.
- - Maintaining high liquidity in our investment portfolio will result in lower net investment income but will ensure our ability to meet contractholder obligations. We will target sales of our spread based products at levels that allow us to avoid sales of investments with significant unrealized losses into distressed or illiquid markets.
- - We expect continued investment spread compression due to credit losses, reduced contractholder funds and maintenance of liquidity.

INVESTMENTS

OVERVIEW AND STRATEGY An important component of our financial results is the return on our investment portfolio. We manage the underlying portfolio based upon the nature of the business and its corresponding liability structure.

The global economy is under significant stress and financial markets continue to experience extreme levels of volatility. Our strategy in 2009 will focus primarily upon mitigating the risks from a potential increase in risk-free interest rates, reducing exposure to certain investment sectors, and maintaining sufficient liquidity and capital. In order to achieve this, we expect to use a combination of reinvestment of the portfolio's significant cash flows, derivatives and other portfolio actions.

Our investment strategy focuses on the total return of assets needed to support the underlying liabilities to achieve return on capital and profitable growth. The portfolio management process begins with a strategic asset allocation model which considers the nature and risk tolerances of the liabilities, as well as the risk and return parameters of the various asset classes in which we invest. This approach is informed by our economic and market outlook, as well as other inputs and constraints including duration, liquidity and capital preservation. Within the ranges set by the strategic asset allocation model, tactical investment decisions are made in consideration of prevailing market conditions.

As a result of decisions in managing our portfolio, we may sell securities during a period in which fair value has declined below amortized cost for fixed income securities or cost for equity securities. For more information, see the Net Realized Capital Gains and Losses section of the MD&A.

During 2008, we developed risk mitigation and return optimization programs as our outlook on the economy changed significantly as conditions deteriorated throughout the year. The risk mitigation and return optimization programs augment earlier actions to reduce investments in real estate and other market sectors as well as to mitigate credit spread risk. At the end of the second quarter of 2008, we had an outlook for continued weakness in the global financial markets and economy including continued volatility in the financial markets, reduced liquidity in certain asset classes and unfavorable economic trends. During the third quarter of 2008, we significantly modified our outlook to a more severe and prolonged downturn. We continue to expect extreme levels of volatility in the financial markets, suppressed liquidity in certain asset classes and further unfavorable global economic conditions. In addition, the potential for market supply and demand imbalances has remained above normal due to the deteriorating credit strength of financial institutions and eroding investor confidence.

Among our risk mitigation and return optimization activities, we have taken the following actions:

- Developed and maintained a tactical positioning in liquid assets and assets that we can sell without generating significant additional realized capital losses.
- Continued to reduce exposure in assets other than those for which we have asserted an intent to hold until recovery where we have credit concerns or where there has been a significant change in facts and circumstances.
- Decreased exposure to financial-related market sectors to \$6.32 billion as of December 31, 2008 from \$9.82 billion as of December 31, 2007, primarily as a result of targeted sales and declines in fair value. Also reduced our short-term investing in financial institutions.
- Decreased exposure to residential and commercial real estate market sectors to \$18.60 billion as of December 31, 2008 from \$24.36 billion as of December 31, 2007 as a result of targeted sales, principal payments and declines in fair value.
- Reduced overall counterparty exposure replacing over-the-counter ("OTC") derivatives transactions with exchange-traded instruments where available.
- In the second half of 2008, we sold \$1.67 billion of government securities and recognized realized capital gains of \$241 million.
- As part of the risk mitigation and return optimization programs, hedges were implemented to mitigate credit spread risk.

Investments for which we changed our intent to hold to recovery as of June 30, 2008 totaled \$2.97 billion and included \$2.64 billion as part of the risk mitigation and return optimization programs and \$329 million related to individual securities. A risk mitigation and return optimization program, approved as of the end of the second quarter of 2008, was designed to reduce our exposure to residential and commercial real estate and the financial-related market sector by approximately \$3 billion of amortized cost, prior to change in intent write-downs. A comprehensive review identified specific investments that could be significantly impacted by continued deterioration in the economy that may be sold. This included a portion of our residential and commercial real estate securities including securities collateralized by residential and commercial mortgage loans, mortgage loans and securities issued by financial institutions.

During the third and fourth quarters of 2008, we sold \$1.26 billion of these securities. On October 1, 2008, it was determined that, due to the financial markets experiencing additional severe deterioration and disruptions, we would be unable to sell certain of the investments identified as part of the programs at a value equal to or greater than our view of their intrinsic values. Approximately \$834 million of these investments were re-designated as intent to hold to recovery. Investments for which we had changed our intent to hold to recovery totaled \$774 million as of December 31, 2008. For a more detailed discussion on securities written down due to a change in intent, see the Net Realized Capital Gains and Losses section of the MD&A.

We continue to monitor the progress of these actions as market and economic conditions develop and will adapt our strategies as appropriate. Our continuing focus is to manage our risks and to position our portfolio to take advantage of market opportunities while attempting to mitigate further adverse effects.

INVESTMENTS OUTLOOK

- - Continuing risk mitigation efforts will focus on reducing exposures to real estate and certain other market sectors, shortening duration of the fixed income portfolio, and managing excess market volatility through our macro hedging program for credit spread risk.
- - Net investment income will decline due to lower asset balances and yields, and the costs of maintaining high liquidity and the risk mitigation programs.
- - Our portfolio continues to generate significant cash flow from maturities, principal and interest receipts which will be available to manage liabilities and take advantage of market opportunities.

PORTFOLIO COMPOSITION The composition of the investment portfolio at December 31, 2008 is presented in the table below. Also see Notes 2 and 6 to the consolidated financial statements for investment accounting policies and

additional information.

PERCENT TO
(\$ IN
MILLIONS)
INVESTMENTS
TOTAL -----

Fixed income
securities
(1) \$ 42,446
71.0%
Mortgage
loans 10,012
16.7 Equity
securities
(2) 82 0.1
Limited
partnership
interests
(3) 1,187
2.0 Short-
term (4)
3,858 6.5
Policy loans
813 1.4
Other 1,374
2.3 -----

----- Total
\$ 59,772
100.0%

=====
=====

-
- (1) Fixed income securities are carried at fair value. Amortized cost basis for these securities was \$49.14 billion.
 - (2) Equity securities are carried at fair value. Cost basis for these securities was \$106 million.
 - (3) We have commitments to invest in additional limited partnership interests totaling \$1.08 billion.
 - (4) Short-term investments are carried at fair value. Amortized cost basis for these investments was \$3.86 billion.

Total investments decreased to \$59.77 billion at December 31, 2008, from \$72.41 billion at December 31, 2007, due to unrealized net capital losses, net reductions in contractholder funds, net realized capital losses, and lower funds associated with collateral received in conjunction with securities lending, partially offset by capital contributions from AIC.

Total investments at amortized cost related to collateral received in connection with securities lending business activities and collateral posted by counterparties related to derivative transactions decreased to \$340 million at December 31, 2008, from \$1.82 billion at December 31, 2007. As of December 31, 2008, these investments are included as a component of short-term investments. At December 31, 2007, these investments were carried at fair value and \$1.57 billion were classified in fixed income securities and \$219 million were classified in short-term investments.

Securities lending activities are primarily used as an investment yield enhancement, and are conducted with third parties such as large banks. We obtain collateral, typically in the form of cash, in an amount generally equal to 102% of the fair value of securities and monitor the market value of the securities loaned on a daily basis with additional collateral obtained as necessary. The cash we receive is invested in short-term and fixed income investments, and an offsetting liability to return the collateral is recorded in other liabilities and accrued expenses.

We obtain fair values of our fixed income and equity securities and exchange traded and non-exchange traded derivative contracts from several sources and methods. For a discussion of these sources and methods, see the Application of Critical Accounting Estimates section of the MD&A.

We may utilize derivative financial instruments to help manage the exposure to interest rate risk, and to a lesser extent currency and credit risks, from the fixed income securities portfolio. For a more detailed discussion of interest rate, currency and credit risks and our use of derivative financial instruments, see the Net realized capital gains and losses and Market Risk

FIXED INCOME SECURITIES See Note 6 of the consolidated financial statements for a table showing the amortized cost, unrealized gains, unrealized losses and fair value for each type of fixed income security for the years ended December 31, 2008 and 2007.

The following table shows fixed income securities by type.

FAIR VALUE AT % TO TOTAL FAIR VALUE AT % TO TOTAL (\$ IN MILLIONS)	DECEMBER 31, 2008	INVESTMENTS DECEMBER 31, 2007	INVESTMENTS

U.S.			
government			
and			
agencies \$	3,687	6.2%	
\$ 3,728			
5.2%			
Municipal	3,308	5.5	
	4,311	6.0	
Corporate	24,269		
	40.6		
	31,735	43.8	
Foreign			
government	2,100	3.5	
	2,185	3.0	
Mortgage-			
backed			
securities			
("MBS")	2,719	4.6	
	3,490	4.8	
CMBS	3,730		
6.2	7,388		
10.2	ABS		
	2,623	4.4	
	5,603	7.7	
Redeemable			
preferred			
stock	10	-	
-	29	--	--

Total			
fixed			
income			
securities			
\$ 42,446			
71.0%	\$		
58,469			
80.7%			
=====			
=====			
=====			
=====			

VALUE COST
VALUE
GAIN/LOSS
AMORTIZED
COST -----

- Non -
zero-
coupon:
Rating (1)
Aaa \$ 42 \$
46 \$ 52 \$
6 113.0%
Aa 829 815
756 (59)
92.8 A 553
553 530
(23) 95.8
Baa 433
435 396
(39) 91.0
Ba or
lower 49
51 35 (16)
68.6 -----

Total \$
1,906 \$
1,900 \$
1,769 \$
(131) 93.1
=====
=====
=====
=====

Zero-
coupon:
Rating (1)
Aaa \$ 147
\$ 42 \$ 39
\$ (3) 92.9
Aa 975 413
289 (124)
70.0 A 771
331 228
(103) 68.9
Baa 3,600
565 330
(235) 58.4

- Total \$
5,493 \$
1,351 \$
886 \$
(465) 65.6
=====
=====
=====
=====

Total:
Rating (1)
(2) Aaa \$
880 \$ 778
\$ 714 \$
(64) 91.8
Aa 1,822
1,247
1,061
(186) 85.1
A 1,340
900 771
(129) 85.7
Baa 4,033

1,000 727
(273) 72.7
Ba or
lower 49
51 35 (16)
68.6 -----

Total (2)
\$ 8,124 \$
3,976 \$
3,308 \$
(668) 83.2
=====

- (1) Moody's equivalent rating will not necessarily tie to ratings distributions from the NAIC due to potential timing differences between the various rating suppliers and the number of external rating agencies used in the determination.
- (2) Includes ARS securities with par value of \$725 million, amortized cost of \$725 million, fair value of \$653 million and unrealized gain/loss of \$(72) million.

The unrealized net capital loss of \$668 million at December 31, 2008 in our municipal bond portfolio was mainly caused by widening credit spreads that affected two main areas in this portfolio: zero-coupon holdings contributing \$465 million of the unrealized losses and student loan ARS contributing \$72 million of the unrealized losses.

Included in our municipal bond portfolio at December 31, 2008 are \$653 million of ARS that have long-term stated maturities, with the interest rate reset based on auctions that generally occur every 7, 28 or 35 days depending on the specific security. This is compared to a balance of ARS at December 31, 2007 of \$866 million, with the decline primarily representing redemptions from calls or refunding proceeds since December 31, 2007. Our holdings primarily have a Moody's or equivalent rating of Aaa. All of our holdings are pools of student loans for which at least 85% of the collateral was insured by the U.S. Department of Education at the time we purchased the security. As of December 31, 2008, \$426 million of our ARS backed by student loans was 100% insured by the U.S. Department of Education, \$154 million was 90% to 99% insured and \$59 million was 80% to 89% insured. All of our student loan ARS holdings are experiencing failed auctions and we receive the failed auction rate or, for those which contain maximum reset rate formulas, we receive the contractual maximum rate. We anticipate that failed auctions may persist and most of our holdings will continue to pay the failed auction rate or, for those that contain maximum rate reset formulas, the maximum rate, as described below. Auctions continue to be conducted as scheduled for each of the securities.

We estimate that approximately 48% of our student loan backed ARS include maximum rate reset formulas with a look back feature whereby if the failed auction rate exceeds an annual contractual maximum rate over a preceding stipulated period, the coupon interest rate is temporarily reset to the maximum rate, which can vary between zero and the failed auction rate. This maximum rate formula causes the reset interest rate on these securities to be lower than the failed auction rate in order to reduce the annual interest rate so that it does not exceed the annual contractual maximum rate. Generally, the annual contractual maximum rate is higher than the historical rates paid on these securities. At December 31, 2008, interest on \$67 million of our ARS has reset using the maximum rate reset formula.

CORPORATE BONDS totaled \$24.27 billion at December 31, 2008. As of December 31, 2008, \$12.36 billion or 50.9% of the portfolio consisted of privately placed securities compared to \$15.57 billion or 49.1% at December 31, 2007. Privately placed securities primarily consist of corporate issued senior debt securities that are in unregistered form and are directly negotiated with the borrower. All privately placed corporate securities are rated by the NAIC based on information provided to them and are also internally rated. Additionally, approximately 40.2% of the privately placed corporate securities in our portfolio are rated by an independent rating agency.

The following table summarizes the corporate fixed income portfolio by

Moody's equivalent rating as of December 31, 2008.

CORPORATE-
PUBLIC ---

(\$ IN
MILLIONS)
NON-HYBRID
HYBRID
TOTAL ----

FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
RATING (1)
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS

Aaa \$ 167
\$ (11) \$ -
- \$ -- \$
167 \$ (11)
Aa 770 18
93 7 863
25 A 4,109
(164) 353
(185)
4,462
(349) Baa
5,568
(627) 164
(165)
5,732
(792) Ba
or lower
676 (218)
9 (12) 685
(230) ----

Total \$
11,290 \$
(1,002) \$
619 \$
(355) \$
11,909 \$
(1,357)
=====

CORPORATE-

PRIVATE --

NON-HYBRID
HYBRID
TOTAL -----

FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
RATING (1)
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS

Aaa \$ 529
\$ 33 \$ --
\$ -- \$ 529
\$ 33 Aa
1,013 (35)
71 (28)
1,084 (63)
A 3,195
(185) 565
(444)
3,760
(629) Baa
6,067
(760) 84
(97) 6,151
(857) Ba
or lower
818 (254)
18 (20)
836 (274)

--- Total
\$ 11,622 \$
(1,201) \$
738 \$
(589) \$
12,360 \$
(1,790)
=====

=====

TOTAL	
CORPORATE	

The unrealized net capital loss of \$3.15 billion at December 31, 2008 is driven primarily by significantly widening credit spreads resulting from deteriorating macro economic conditions and continued credit market deterioration. Credit spread widening particularly affected our non-hybrid Baa and lower rated corporate bond holdings, contributing to approximately \$1.86 billion of the unrealized net capital loss. The other significant driver of unrealized net capital losses in our corporate bond portfolio is from hybrid securities, contributing \$944 million of the unrealized loss. While these securities are generally issued by highly rated financial institutions, they have structural features which make them more sensitive to credit market deterioration. Specifically, features allowing coupon deferral and the extension of call dates have severely impacted prices as the global financial system undergoes significant stress.

The following table shows additional details of our hybrid securities reported in corporate fixed income securities.

UNITED
KINGDOM
EUROPE (NON-
UK)
ASIA/AUSTRALIA
NORTH AMERICA
TOTAL -----

- -----

(\$ IN
MILLIONS)
FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
FAIR
UNREALIZED
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS
VALUE
GAIN/LOSS ---

Tier 1:
Public \$ 82 \$
(61) \$ 73 \$
(77) \$ 17 \$
(8) \$ 232 \$
(210) \$ 404 \$
(356) Private
61 (96) 226
(244) 167
(111) 124
(116) 578
(567) -----

299 (321) 184
 (119) 356
 (326) 982
 (923) Tier 2:
 Public 61 (4)
 111 10 32 (2)
 10 (3) 214 1
 Private 8 (3)
 50 (6) 103
 (13) -- --
 161 (22) ----
 -- -----

 ----- 69 (7)
 161 4 135
 (15) 10 (3)
 375 (21)
 Total hybrids
 Public 143
 (65) 184 (67)
 49 (10) 242
 (213) 618
 (355) Private
 69 (99) 276
 (250) 270
 (124) 124
 (116) 739
 (589) -----

 -- Total \$
 212 \$ (164) \$
 460 \$ (317) \$
 319 \$ (134) \$
 366 \$ (329) \$
 1,357 \$ (944)

=====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

Our portfolio of privately placed securities are broadly diversified by issuer, industry sector, and by country. The portfolio is made up of approximately 551 issues with an average security value of approximately \$22 million. Privately placed corporate obligations generally benefit from increased yields and structural security features such as financial covenants and call protections that provide investors greater protection against credit deterioration, reinvestment risk or fluctuations in interest rates than those typically found in publicly registered debt securities. Additionally, investments in these securities are made after extensive due diligence of the issuer, typically including direct discussions with senior management and on-site visits to company facilities. Ongoing monitoring includes direct periodic dialog with senior management of the issuer and continuous monitoring of operating performance and financial position. Every issue is internally rated with a formal rating affirmation approximately once a year.

FOREIGN GOVERNMENT securities totaled \$2.10 billion, with 94.6% rated investment grade, at December 31, 2008.

CERTAIN COLLATERALIZED SECURITIES are detailed in the following table by Moody's equivalent rating as of December 31, 2008.

FAIR VALUE AT
 DECEMBER 31,
 % TO TOTAL Ba

OR (\$ IN
 MILLIONS)
 2008
 INVESTMENTS
 Aaa Aa A Baa
 LOWER -----

 MBS U.S.
 Agency \$
 1,881 3.2%
 100.0% -- --
 -- -- Prime
 523 0.9 94.6
 3.1% -- 2.3%
 -- Alt-A 315
 0.5 78.7 8.0
 -- 2.2 11.1%

 Total MBS \$
 2,719 4.6%
 =====
 CMBS CMBS \$
 3,703 6.2%
 90.9 8.0 0.9%
 0.2 --
 Commercial
 real estate
 collateralized
 debt
 obligations
 ("CRE CDO")
 27 -- -- 29.6
 37.1 29.6 3.7

 Total CMBS \$
 3,730 6.2%
 =====
 ABS ABS RMBS
 non-insured \$
 1,005 1.7%
 41.5 36.2
 10.0 4.4 7.9
 ABS RMBS
 insured 243
 0.4 1.7 18.1
 2.9 50.2 27.1

 Total ABS
 RMBS 1,248
 2.1 33.7 32.7
 8.7 13.3 11.6
 Asset-backed
 collateralized
 debt
 obligations
 ("ABS CDO") 6
 -- -- -- -- --
 - 100.0 -----
 -- ----- Total
 asset-backed
 securities
 collateralized
 by sub-prime
 residential
 mortgage
 loans 1,254
 2.1 Other
 collateralized
 debt
 obligations:
 Cash flow CLO
 497 0.8 51.3
 21.2 19.7 5.8
 2.0 Synthetic
 CDO 47 0.1
 6.4 31.9 --
 46.8 14.9
 Trust

preferred CDO			
73	0.1	1.4	
76.7	15.1	4.1	
2.7	Market		
value CDO	26		
0.1	--	30.8	
15.4	7.7	46.1	
Project			
finance CDO			
39	0.1	--	
28.2	51.3		
20.5	--	CDOs	
that invest			
in other CDOs			
("CDO			
squared")	9	-	
-	--	55.6	
44.4	--		
Collateralized			
bond			
obligations			
21	--	--	--
-	57.2	42.8	
Other CLO	40		
0.1	100.0	--	
--	--	--	--
----	----	----	----
Total other			
collateralized			
debt			
obligations			
752	1.3	39.8	
25.9	18.4		
10.6	5.3	----	----
----	----	----	----
Other asset-			
backed			
securities			
617	1.0	30.8	
9.9	29.7	20.4	
9.2	-----	-	
---	Total ABS		
\$ 2,623	4.4%		
=====	=====		

During 2008, certain financial markets continued to experience price declines due to market and liquidity disruptions. We experienced this illiquidity and disruption in certain of our MBS, CMBS and ABS fixed income securities, particularly in our Prime residential mortgage-backed securities ("Prime"), Alt-A, CMBS, CRE CDO, ABS RMBS, ABS CDO, and other collateralized debt obligations ("other CDO") portfolios. These portfolios totaled \$6.57 billion or approximately 11% of our total investments at December 31, 2008. Other securities markets, including certain other asset-backed and real estate-backed securities markets, also experienced illiquidity, but to a lesser degree.

We determine the fair values of securities comprising these illiquid portfolios by obtaining information from an independent third-party valuation service provider and brokers. We confirmed the reasonableness of the fair value of these portfolios as of December 31, 2008 by analyzing available market information including, but not limited to, collateral quality, anticipated cash flows, credit enhancements, default rates, loss severities, securities' relative position within their respective capital structures, and credit ratings from statistical rating agencies.

The following table summarizes our illiquid portfolios as of December 31, 2008.

AMORTIZED
COST FAIR
VALUE AS
PAR
AMORTIZED
AS A
PERCENT
FAIR A
PERCENT OF

\$ (55)
 Alt-A 99
 (81) CMBS
 CMBS 857
 (1,623)
 CRE CDO --
 -- ABS ABS
 RMBS 501
 (618) ABS
 CDO 5 (3)
 Other CDO
 449
 (1,044) --

 ---- Total
 \$ 1,960 \$
 (3,424)
 =====
 =====

We continue to believe that the unrealized losses on these securities are not predictive of the ultimate performance of the underlying collateral. In the absence of further deterioration in the collateral relative to our positions in the securities' respective capital structures, which could be other than temporary, the unrealized losses should reverse over the remaining lives of the securities.

The cash flows of the underlying mortgages or collateral for MBS, CMBS (including CRE CDO) and ABS are generally applied in a pre-determined order and are designed so that each security issued qualifies for a specific original rating. The security issue is typically referred to as the "class". For example, the "senior" portion or "top" of the capital structure which would originally qualify for a rating of Aaa is referred to as the "Aaa class" and typically has priority in receiving the principal repayments on the underlying mortgages. In a sequential structure, underlying collateral principal repayments are directed to the most senior rated Aaa class in the structure until paid in full, after which principal repayments are directed to the next most senior Aaa class in the structure until it is paid in full. Although the various Aaa classes may receive principal sequentially, they may share any losses from the underlying collateral on a pro-rata basis after losses are absorbed by classes with lower original ratings or what may be referred to as more "junior" or "subordinate" securities in the capital structure. The underlying mortgages have fixed interest rates, variable interest rates (such as adjustable rate mortgages ("ARM")) or are hybrid, meaning that they contain features of both fixed and variable rate mortgages.

MBS totaled \$2.72 billion, with 98.7% rated investment grade, at December 31, 2008. The MBS portfolio is subject to interest rate risk since price volatility and the ultimate realized yield are affected by the rate of prepayment of the underlying mortgages. The credit risk associated with MBS is mitigated due to the fact that 69.2% of the portfolio consists of securities that were issued by, or have underlying collateral that is guaranteed by, U.S. government agencies or U.S. government sponsored entities ("U.S. Agency").

PRIME are collateralized by residential mortgage loans issued to prime borrowers. The following table shows our Prime portfolio as of December 31, 2008 by vintage year, based upon our participation in the capital structure.

(\$ IN
 MILLIONS)
 VINTAGE YEAR

 ---- CAPITAL
 STRUCTURE
 FAIR
 AMORTIZED
 UNREALIZED
 CLASSIFICATION
 (1) 2007 2006
 2005 PRE-2005
 VALUE COST
 (2) GAIN/LOSS

VALUE	COST
(2) GAIN/LOSS	

Aaa - Fixed rate \$ 25 \$	
22 \$ 89 \$ 132	
\$ 268 \$ 359 \$	
(91) Aaa - Hybrid -- --	
-- 5 5 9 (4)	
Aaa - Option adjustable rate mortgage	
-- -- -- 1 1	
2 (1) Aa - Fixed rate --	
7 2 -- 9 8 1	
Aa - Option adjustable rate mortgage	
-- -- 2 9 11	
14 (3) A and lower -- 14 7	
-- 21 40 (19)	

----- Total \$	
25 \$ 43 \$ 100	
\$ 147 \$ 315 \$	
432 \$(117)	
=====	
=====	
=====	
=====	
=====	
=====	
=====	

- (1) May not be consistent with current ratings due to downgrades.
- (2) Amortized cost includes other-than-temporary impairment charges, as applicable.

CMBS totaled \$3.73 billion, all of which were rated investment grade, at December 31, 2008. The CMBS portfolio is subject to credit risk, but unlike other structured securities, is generally not subject to prepayment risk due to protections within the underlying commercial mortgages whereby borrowers are effectively restricted from prepaying their mortgages due to changes in interest rates. Approximately 92.0% of the CMBS investments are structured securities collateralized by pools of commercial mortgages, broadly diversified across property types and geographical area.

The following table shows our CMBS portfolio, excluding CRE CDO, at December 31, 2008 by vintage year, based upon our participation in the capital structure.

(\$ IN MILLIONS)	CAPITAL STRUCTURE PAR	AMORTIZED FAIR UNREALIZED CLASSIFICATION	(1) VALUE COST (2) VALUE GAIN/LOSS
-----	-----	-----	-----
-----	-----	-----	-----
-----	-----	-----	-----
Aaa 2007:			
Super senior			

(3) \$ 383 \$
 379 \$ 263 \$
 (116)
 Mezzanine
 senior (4)
 130 122 58
 (64)
 Subordinated
 senior (5)
 596 569 166
 (403) Other
 (6) 21 22 9
 (13) ----- -

 ----- 1,130
 1,092 496
 (596) 2006:
 Super senior
 (3) 102 102
 64 (38)
 Mezzanine
 senior (4) 81
 77 41 (36)
 Subordinated
 senior (5)
 314 301 94
 (207) Other
 (6) 55 56 37
 (19) ----- -

 ----- 552
 536 236 (300)
 2005: Super
 senior (3)
 309 311 245
 (66)
 Mezzanine
 senior (4) 22
 22 13 (9)
 Subordinated
 senior (5)
 108 115 48
 (67) Other
 (6) 95 95 70
 (25) ----- -

 ----- 534
 543 376 (167)
 Pre-2005 (7):
 2,081 2,108
 1,896 (212) -

 - Aaa total
 4,297 4,279
 3,004 (1,275)
 Aa 1,108
 1,176 520
 (656) A 345
 222 169 (53)
 Baa 35 8 8 --
 Ba or lower 2
 2 2 -- -----

 ----- Total
 CMBS \$5,787
 \$5,687 \$3,703
 \$(1,984)
 =====
 =====
 =====

-
- (1) May not be consistent with current ratings due to upgrades and downgrades.
 - (2) Amortized cost includes other-than-temporary impairment charges, as applicable.
 - (3) Most senior of the Aaa rated tranches, typically has a high level of credit enhancement of approximately 30%, meaning actual losses in the deal have to reach 30% before incurring a first dollar loss.
 - (4) Middle Aaa rated tranche, typically having credit enhancement of

ABS RMBS includes securities that are collateralized by mortgage loans issued to borrowers that cannot qualify for Prime or Alt-A financing terms due in part to weak or limited credit history. It also includes securities that are collateralized by certain second lien mortgages regardless of the borrower's credit history. \$957 million or 76.7% of the ABS RMBS portfolio consisted of securities that were issued during 2005, 2006 and 2007. At December 31, 2008, 37.5% of securities issued during 2005, 2006 and 2007 were rated Aaa, 26.7% rated Aa, 7.0% rated A, 14.4% rated Baa and 14.4% rated Ba or lower.

The following table presents additional information about our ABS RMBS portfolio including a summary by first and second lien collateral at December 31, 2008.

% TO TOTAL	
(\$ IN MILLIONS)	
FAIR VALUE INVESTMENTS	

- ABS RMBS	
First lien:	
Fixed rate(1) \$	
375	0.6%
Variable rate(1)	
652	1.1
	--

--- Total first lien(2)	
1,027	1.7
Second lien:	
Insured	
166	0.3
Other	55
0.1	-----

Total second lien(3)	
221	0.4
	--

--- Total ABS RMBS \$	
1,248	2.1%
	=====
	=====

-
- (1) Fixed rate and variable rate refer to the primary interest rate characteristics of the underlying mortgages at the time of issuance.
 - (2) The credit ratings of the first lien ABS RMBS were 38.1% Aaa, 37.8% Aa, 10.0% A, 6.0% Baa and 8.1% Ba or lower at December 31, 2008.
 - (3) The credit ratings of the second lien ABS RMBS were 13.6% Aaa, 9.0% Aa, 2.2% A, 47.1% Baa and 28.1% Ba or lower at December 31, 2008.

The following table includes first lien non-insured ABS RMBS by vintage year and the interest rate characteristics of the underlying mortgage product.

VARIABLE	FIXED FAIR	AMORTIZED	UNREALIZED	(\$ IN	MILLIONS)	RATE RATE	VALUE COST	(1)
----------	------------	-----------	------------	--------	-----------	-----------	------------	-----

48 3 23
 166 386
 (220) ----

 Total
 insured
 ABS RMBS \$
 122 \$ 55 \$
 35 \$ 31 \$
 243 \$ 499
 \$ (256)
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

(1) Amortized cost includes other-than-temporary impairment charges, as applicable.

Other CDO totaled \$752 million, with 94.7% rated investment grade, at December 31, 2008. Other CDO consist primarily of obligations secured by high yield and investment grade corporate credits including cash flow CLO, synthetic CDO, trust preferred CDO, market value CDO, project finance CDO, CDO squared, collateralized bond obligations and other CLO.

The following table presents realized and unrealized capital gains and losses and principal transactions on our Other CDO portfolio for the year ended December 31, 2008.

REALIZED
 CAPITAL GAINS
 AND LOSSES (1)
 PRINCIPAL
 TRANSACTIONS --

 IMPAIRMENT
 UNREALIZED
 PRINCIPAL (\$ IN
 MILLIONS) SALES
 WRITE-DOWNS
 GAINS/LOSSES
 SOLD RECEIVED
 ACQUIRED -----

 ----- OTHER
 CDO Cash flow
 CLO \$ 1 \$ (59)
 \$ (685) \$ 7 \$ 5
 \$ 11 Synthetic
 CDO -- (186)
 (160) 2 -- --
 Trust preferred
 CDO -- (28)
 (91) -- 11 --
 Market value
 CDO 1 (33) (63)
 1 -- -- Project
 finance CDO --
 -- (34) -- -- --
 - CDO squared -
 - -- (68) -- --
 --
 Collateralized
 bond
 obligations --
 -- (5) 1 1 --

\$ 211 \$ 497 \$
 1,182 \$ (685)
 =====
 =====
 =====
 =====
 =====
 =====
 =====

- (1) May not be consistent with current ratings due to downgrades.
 (2) Amortized cost includes other-than-temporary impairment charges, as applicable.

Synthetic CDO primarily consist of a portfolio of corporate credit default swaps ("CDS") which are collateralized by Aaa rated LIBOR-based securities (i.e. "fully funded" synthetic CDO). Our synthetic CDO collateral primarily is actively managed by an external manager monitoring the CDS selection and performance. The following table shows our synthetic CDO at December 31, 2008 by vintage year, based upon our participation in the capital structure.

(\$ IN MILLIONS)
 VINTAGE YEAR ---

 CAPITAL
 STRUCTURE FAIR
 AMORTIZED
 UNREALIZED
 CLASSIFICATION(1)
 2007 2006 VALUE
 COST (2)
 GAIN/LOSS -----

 ----- Aaa
 \$25 \$-- \$25 \$ 85
 \$ (60) Aa 6 16
 22 122 (100) ---

 --- Total \$31
 \$16 \$47 \$207
 \$(160) === ===
 === =====

- (1) May not be consistent with current ratings due to downgrades.
 (2) Amortized cost includes other-than-temporary impairment charges, as applicable.

Trust preferred CDO underlying assets are primarily comprised of portfolios of preferred securities issued by a diversified portfolio of domestic banks and other financial institutions. The underlying collateral for our trust preferred CDO portfolio is not actively managed and is diversified by issuer, predominately regional banks, with a small percentage of insurance companies.

Market value CDO are structurally similar to cash flow CLO. The primary difference is that the market value of the underlying assets is managed in order to enhance returns and the structure is governed by market value based tests. The managers are also offered more flexibility to purchase other asset types including secured leveraged loans, public and private high yield bonds, structured products, mezzanine investments, and equities.

Project finance CDO underlying assets are primarily below investment grade senior secured project finance loans and energy finance investments.

CDO squared transactions are CDOs where the underlying assets are primarily other cash flow CLO tranches, typically with an average rating of Baa.

Other asset-backed securities totaled \$617 million at December 31, 2008 and consist primarily of investments secured by portfolios of credit card loans, auto loans, student loans and other consumer and corporate obligations. As of December 31, 2008, the net unrealized losses on these securities were \$164 million. Additionally, 22.2% of the other asset-backed securities that are rated Aaa, Aa, A and Baa were insured by four bond insurers. During 2008, we sold \$102 million of these securities recognizing a gain of \$1 million. In addition, we acquired \$28 million of securities during 2008. We also collected \$73 million of principal repayments consistent with the expected cash flows during 2008.

Aa 308
18.3 A 488
29.0 A 837
49.8 Baa
581 34.6
Baa 458
27.3 -----

Total
municipal
bonds \$
1,680
100.0 % \$
1,680
100.0 %
=====

=====
=====
=====

ABS RMBS
Aaa \$ 4
1.6 % Aaa
\$ 6 2.5 %
Aa 44 18.1
Aa 19 7.8
A 7 2.9 A
31 12.8
Baa 122
50.2 Baa
13 5.3 Ba
39 16.1 Ba
20 8.2 B
10 4.1 B
13 5.3 Caa
or lower
17 7.0 Caa
or lower
11 4.6
Rating
without
Insurance
Guarantee
not
provided
("NA") --
-- NA 130
53.5 -----

Total ABS
RMBS \$ 243
100.0 % \$
243 100.0
%
=====

=====
=====
=====

OTHER
ASSET-
BACKED
SECURITIES
Aaa \$ 62
36.0 % Aaa
\$ -- -- %
Aa 46 26.7
Aa -- -- A
-- -- A 8
4.7 Baa 29
16.9 Baa
69 40.1 Ba
17 9.9 Ba
-- -- NA
18 10.5 NA
95 55.2 --

- Total
other
asset-
backed
securities
\$ 172
100.0 % \$
172 100.0
%
=====

MORTGAGE LOANS Our mortgage loan portfolio was \$10.01 billion and \$9.90 billion at December 31, 2008 and 2007, respectively, and comprised primarily loans secured by first mortgages on developed commercial real estate. Geographical and property type diversification are key considerations used to manage our exposure. The portfolio is diversified across several property types. Our largest exposure to any metropolitan area is also highly diversified, with the largest exposure not exceeding 10% of the portfolio. The average debt service coverage ratio represents the amount of cash flows available from the property to meet the borrower's principal and interest payment obligations.

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The average debt service coverage ratio of the portfolio as of December 31, 2008 was approximately 2.0, and only approximately 3.0% of the mortgage loan portfolio had a debt service coverage ratio under 1.0.

We closely monitor our commercial mortgage loan portfolio on a loan-by-loan basis. Loans with an estimated collateral value less than the loan balance, as well as loans with other characteristics indicative of higher than normal credit risks, are reviewed at least quarterly for purposes of establishing valuation allowances and placing loans on non-accrual status as necessary. The underlying collateral values are based upon either discounted property cash flow projections or a commonly used valuation method that utilizes a one-year projection of expected annual income divided by a market based expected rate of return. We had \$3 million of realized capital losses related to valuation allowances on mortgage loans for the year ended December 31, 2008 and had no realized capital losses related to valuation allowances on mortgage loans for the year ended December 31, 2007. Additionally, realized capital losses due to changes in intent to hold mortgage loans to maturity totaled \$73 million and \$28 million for the years ended December 31, 2008 and 2007, respectively. For further detail, see Note 6 to the consolidated financial statements.

EQUITY SECURITIES Equity securities include common stocks, real estate investment trust equity investments and non-redeemable preferred stocks. The equity securities portfolio was \$82 million at December 31, 2008 compared to \$102 million at December 31, 2007. The decrease is primarily attributable to higher unrealized losses and sales of equity securities with realized gains of \$4 million and realized losses of \$12 million. Gross unrealized gains totaled \$1 million at December 31, 2008 compared to \$5 million at December 31, 2007. Gross unrealized losses totaled \$25 million at December 31, 2008 compared to \$5 million at December 31, 2007.

LIMITED PARTNERSHIP INTERESTS consist of investments in private equity/debt funds, real estate funds and hedge funds. The overall limited partnership interests portfolio is well diversified across a number of metrics including fund sponsors, vintage years, strategies, geography (including international), and company/property types.

The following table presents information about our limited partnership interests as of December 31, 2008.

PRIVATE
EQUITY/
REAL
ESTATE
HEDGE (\$
IN
MILLIONS)
DEBT FUNDS
FUNDS
FUNDS
TOTAL ----


```

-----
---
---- COST
METHOD OF
ACCOUNTING
("COST") $
384 $ 175
$ 1 $ 560
EQUITY
METHOD OF
ACCOUNTING
("EMA")
345 218 64
627 -----
--
-----
--- TOTAL
$ 729 $
393 $ 65 $
1,187
=====
=====
=====
=====
NUMBER OF
SPONSORS
68 32 2
NUMBER OF
INDIVIDUAL
FUNDS 118
54 3
LARGEST
EXPOSURE
TO SINGLE
FUND $ 22
$ 31 $ 36

```

Our aggregate limited partnership exposure represented 2.0% and 1.4% of total invested assets as of December 31, 2008 and December 31, 2007, respectively.

The following table shows the income from our limited partnership interests by fund type and accounting classification for the years ended December 31.

```

2008 2007
-----
-----
-----
-----
-- ($ IN
MILLIONS)
COST
EMA(1)
TOTAL COST
EMA TOTAL
-----
-----
-----
-----
-----
Private
equity/debt
funds $ 12
$ 43 $ 55
$ 27 $ 19
$ 46 Real
estate
funds 3
(26) (23)
10 24 34
Hedge
funds --
(17) (17)
-- 7 7 ---
-----
-----
-----
----- Total

```

\$ 15 \$ --
 \$ 15 \$ 37
 \$ 50 \$ 87
 =====
 =====
 =====
 =====
 =====

(1) Beginning in the fourth quarter of 2008, income from limited partnerships accounted for on the equity method of accounting ("EMA LP") is reported in realized capital gains and losses. EMA LP income for periods prior to the fourth quarter of 2008 is reported in net investment income.

Income from limited partnership interests was \$15 million for 2008 and \$87 million for 2007. The decrease in 2008 is primarily related to losses from EMA LP resulting from reduced valuations on the net asset value of the partnerships. Further, income on EMA LP is recognized on a delay due to the availability of the related financial statements. The recognition of income on hedge funds is primarily on a one-month delay and the income recognition on private equity/debt funds and real estate funds are generally on a three-month delay as of December 31, 2008. As such, the income recognized through December 31, 2008 for EMA LP may not include the full impact for calendar year investment market changes as they will ultimately impact the valuation of the underlying assets or

liabilities within the partnerships. Limited partnership interests accounted for under the cost method of accounting recognize income only upon cash distributions by the partnership.

SHORT-TERM INVESTMENTS Our short-term investment portfolio was \$3.86 billion and \$386 million at December 31, 2008 and 2007, respectively. The increase in short-term investments was primarily due to liquidity management actions. We invest available cash balances primarily in taxable short-term securities having a final maturity date or redemption date of less than one year.

POLICY LOANS Our policy loan portfolio was \$813 million and \$770 million at December 31, 2008 and 2007, respectively. Policy loans are carried at the unpaid principal balances.

OTHER INVESTMENTS Our other investments as of December 31, 2008 are comprised of \$981 million of bank loans, \$138 million of certain derivatives, including credit default swaps, and \$255 of other investments. Bank loans are comprised primarily of senior secured corporate loans and are carried at amortized cost. Other investments are comprised primarily of intercompany notes issued by an unconsolidated affiliate.

CREDIT DEFAULT SWAPS ("CDS") are utilized for both buying and selling credit protection against a specified credit event. In selling protection, CDS are used to replicate fixed income securities and to complement the cash market when credit exposure to certain issuers is not available or when the derivative alternative is less expensive than the cash market alternative. We are not selling protection to acquire revenues as a business activity. When buying protection, the objective is to mitigate credit risk on fixed income holdings in our portfolio. Credit risk includes both default risk and market value exposure due to spread widening. CDS typically have a five-year term. The following table shows the CDS notional amounts and fair value of protection bought or sold as of December 31, 2008.

FAIR VALUE (\$
 IN MILLIONS)
 NOTIONAL FAIR
 TO NOTIONAL
 AMOUNTS VALUE
 (1) AMOUNT --

 Buying
 protection
 (recoverable)
 Single name \$
 422 \$ 8 1.9%
 Index 723 23
 3.2 -----

----- Total
buying
protection \$
1,145 \$ 31
2.7
=====

Selling
protection
(payable)
Single name \$
272 \$ (25)
(9.2) First-
to-default
245 (48)
(19.6) -----

Total selling
protection \$
517 \$ (73)
(14.1)
=====

- (1) Included as a component of other investments and other liabilities and accrued expenses on the Consolidated Statements of Financial Position.

In buying and selling protection CDS, we buy or sell credit protection on an identified single name, a basket of names in a first-to-default ("FTD") structure or credit derivative index ("CDX") that is generally investment grade, and in return pay or receive periodic premiums through expiration or termination of the agreement. With single name CDS, the premium or credit spread generally corresponds to the difference between the yield on the referenced name's public fixed maturity cash instruments and swap rates, at the time the agreement is executed. With FTD baskets, because of the additional credit risk inherent in a basket of named credits, the premium generally corresponds to a high proportion of the sum of the credit spreads of the names in the basket and correlation between the names. CDX index is utilized to take a position on multiple (generally 125) credit entities. Credit events are typically defined as bankruptcy, failure to pay, or restructuring, depending on the nature of the reference credit. If a credit event occurs, we settle with the counterparty, either through physical settlement or cash settlement. In a physical settlement, a reference asset is delivered by the buyer of protection to the seller of protection, in exchange for cash payment at par, while in a cash settlement, the seller pays the difference between par and the prescribed value of the reference asset. When such an event occurs in a single name or FTD basket (for FTD, the first such event occurring for any one name in the basket), the contract terminates at time of settlement. For CDX index, the reference entity's name incurring the credit event is removed from the index while the contract continues until expiration. The maximum payout on a CDS is the contract notional amount. For all CDS, once a credit event and settlement has occurred, there may be subsequent recoveries. Recovery amounts, if any, vary and they may reduce the ultimate amount of net gain or loss.

UNREALIZED GAINS AND LOSSES See Note 6 of the consolidated financial statements for further disclosures regarding unrealized losses on fixed income and equity securities and factors considered in determining whether securities are other-than-temporarily impaired. The unrealized net capital losses totaled \$6.70 billion as of December 31, 2008, compared to unrealized net capital gains of \$417 million at December 31, 2007 as a result of significantly widening credit spreads and, to a much lesser extent, declining equity markets.

The following table presents unrealized net capital gains and losses, pre-tax and after-tax at December 31.

(\$ IN
MILLIONS)
2008 2007

U.S.
GOVERNMENT
AND
AGENCIES \$

895 \$ 880
MUNICIPAL
(668) 76
CORPORATE
(3,147)
111
FOREIGN
GOVERNMENT
448 371
MBS (204)
(9) CMBS
(1,982)
(310) ABS
(2,026)
(670)
REDEEMABLE
PREFERRED
STOCK (6)

---- FIXED
INCOME
SECURITIES
(6,690)
449 EQUITY
SECURITIES
(24) --
SHORT-TERM
INVESTMENTS
3 --
DERIVATIVES
14 (32) --

UNREALIZED
NET
CAPITAL
GAINS AND
LOSSES,
PRE-TAX
(6,697)
417 -----

AMOUNTS
RECOGNIZED
FOR:
INSURANCE
RESERVES
(1) (378)
(1,059)
DAC AND
DSI (2)
3,493 513

AMOUNTS
RECOGNIZED
3,115
(546)
DEFERRED
INCOME
TAXES
1,245 45 -

UNREALIZED
NET
CAPITAL
GAINS AND
LOSSES,
AFTER-TAX
\$ (2,337)
\$ (84)
=====

(1) The insurance reserves adjustment represents the amount by which the reserve balance would increase if the net unrealized gains

(1) (6) --
 (413) 3,151
 Capital goods
 -- -- (39)
 (156) (46)
 (28) -- --
 (269) 1,698
 Basic
 industry --
 (4) (13) (95)
 (23) (32) --
 -- (167)
 1,096
 Transportation
 -- -- (39)
 (76) (40) (1)
 -- -- (156)
 822
 Communications
 -- -- (6)
 (99) (41) (9)
 -- -- (155)
 1,072 Energy
 -- (3) (6)
 (101) (8) (3)
 -- -- (121)
 901
 Technology
 (2) (2) (15)
 (49) (5) (4)
 -- -- (77)
 513 Other --
 -- (71) (259)
 (8) -- -- --
 (338) 820 ---

 Total
 corporate
 fixed income
 portfolio
 (22) (96)
 (1,165)
 (1,759) (395)
 (101) (16)
 (1) (3,555)
 17,125 -----

 ----- ABS
 (243) (560)
 (566) (467)
 (86) (59)
 (39) (14)
 (2,034) 2,443
 CMBS (1,311)
 (642) (24)
 (15) -- -- --
 -- (1,992)
 3,547
 Municipal
 (72) (197)
 (137) (274) -
 - (16) -- --
 (696) 2,658
 MBS (200)
 (17) -- (26)
 (10) (10) --
 -- (263) 957
 Foreign
 government --
 -- (4) (21)

(17) (23) --
 -- (65) 318
 Redeemable
 preferred
 stock -- -- --
 - (6) -- -- --
 - -- (6) 9
 U.S.
 government
 and agencies

 81 -----

--- Total
 fixed income
 securities \$
 (1,848) \$
 (1,512) \$
 (1,896) \$
 (2,568) \$
 (508) \$ (209)
 \$ (55) \$ (15)
 \$ (8,611) \$
 27,138

=====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

Rating % to
 total
 unrealized
 loss 21.5%
 17.6% 22.0%
 29.8% 5.9%
 2.4% 0.6%
 0.2% 100.0%

=====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

(1) Moody's equivalent rating will not necessarily tie to ratings distributions from the NAIC due to potential timing differences between the various rating suppliers and the number of external rating agencies used in the determination.

The scheduled maturity dates for fixed income securities at December 31, 2008 are shown below. Actual maturities may differ from those scheduled as a result of prepayments by the issuers.

FIXED
 INCOME
 SECURITIES
 IN GROSS
 FIXED
 INCOME
 SECURITIES
 IN GROSS
 UNREALIZED
 GAIN
 POSITION
 UNREALIZED

(I):
 Unrealized
 loss less
 than 20%
 of cost(1)
 Number of
 issues
 1,933 113
 4 2,050
 2,403 227
 9 2,639
 Fair value
 \$ 18,433 \$
 622 \$ 31 \$
 19,086 \$
 22,615 \$
 1,517 \$ 64
 \$ 24,196

Unrealized
 \$ (1,627)
 \$ (82) \$
 (3) \$
 (1,712) \$
 (1,129) \$
 (106) \$
 (5) \$
 (1,240)

Category
 (II):
 Unrealized
 loss
 greater
 than or
 equal to
 20% of
 cost for a
 period of
 less than
 6

consecutive
 months (1)
 Number of
 issues 853
 183 35
 1,071 156
 18 -- 174
 Fair value
 \$ 6,346 \$
 802 \$ 24 \$
 7,172 \$
 945 \$ 107
 \$ -- \$
 1,052

Unrealized
 \$ (4,442)
 \$ (553) \$
 (22) \$
 (5,017) \$
 (514) \$
 (62) \$ --
 \$ (576)

Category
 (III):
 Unrealized
 loss
 greater
 than or
 equal to
 20% of
 cost for a
 period of
 6 or more
 consecutive
 months,
 but less
 than 12
 consecutive
 months (1)
 Number of
 issues 193
 19 -- 212

losses \$
 (7,824) \$
 (787) \$
 (25) \$
 (8,636) \$
 (1,643) \$
 (168) \$
 (5) \$
 (1,816)
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

-
- (1) For fixed income securities, cost represents amortized cost.
 - (2) At December 31, 2008, 95.9% of the fixed income securities portfolio was rated investment grade compared to 95.5% at December 31, 2007.

The largest individual unrealized loss was \$9 million for category (I), \$61 million for category (II), \$38 million for category (III) and \$27 million for category (IV) as of December 31, 2008.

Categories (I) and (II) have generally been adversely affected by overall economic conditions including interest rate increases and the market's evaluation of certain sectors. The degree to which and/or length of time that the securities have been in an unrealized loss position does not suggest that these securities pose a high risk of being other-than-temporarily impaired.

Categories (III) and (IV) have primarily been historically adversely affected by industry and issue specific, or issuer specific conditions.

At December 31, 2008, Category (III) for fixed income was comprised primarily of fair values of \$246 million of ABS RMBS, \$130 million for cash flow CLO, \$130 million of corporate private and \$94 million of CMBS, for a total of \$600 million with unrealized losses of \$317 million, \$416 million, \$139 million and \$407 million, respectively, for a total of \$1.28 billion of unrealized losses. No other security type individually represents more than \$56 million of fair value within this category.

Of the unrealized losses on below investment grade securities, 19.3% were in significant unrealized loss positions (greater than or equal to 20% of amortized cost) for six or more consecutive months prior to December 31,

2008. Included among the securities rated below investment grade are high-yield bonds and securities that were investment grade when originally acquired. We mitigate the credit risk of investing in below investment grade fixed income securities by limiting the percentage of our fixed income portfolio invested in such securities through diversification of the portfolio, active credit monitoring and portfolio management activities. We continue to believe that the unrealized losses on these securities are not predictive of the ultimate performance.

Whenever our initial analysis indicates that a fixed income security's unrealized loss of 20% or more for at least 36 months or any equity security's unrealized loss of 20% or more for at least 12 months is temporary, additional evaluations and management approvals are required to substantiate that a write-down is not appropriate.

The following table contains the individual securities with the largest unrealized losses as of December 31, 2008. No other fixed income or equity security had an unrealized loss greater than \$28 million or 0.3% of the total unrealized loss on fixed income and equity securities.

FAIR VALUE
 UNREALIZED
 FAIR NAIC
 UNREALIZED
 HIERARCHY
 (\$ IN
 MILLIONS)
 LOSS VALUE
 RATING LOSS

FAIR A
 PERCENT OF
 BANK LOAN
 VALUE (1)
 COST (1)
 PAR VALUE
 VALUE PAR
 VALUE
 PORTFOLIOS

Restructured
 \$ 71 \$ 57
 80.3% \$ 57
 80.3% 0.1%
 Problem 837
 188 22.5
 147 17.6
 0.3
 Potential
 problem
 1,194 432
 36.2 297
 24.9 0.7 --

Total net
 carrying
 value \$
 2,102 \$ 677
 32.2 \$ 501
 23.8 1.1%

=====
 =====
 =====
 =====

Cumulative
 write-
 downs
 recognized
 (2) \$ 1,294

=====
 (\$ IN
 MILLIONS)
 2007 -----

--- PERCENT
 OF
 AMORTIZED
 TOTAL FIXED
 COST AS A
 FAIR VALUE
 AS INCOME
 AND PAR
 AMORTIZED
 PERCENT OF
 FAIR A
 PERCENT OF
 BANK LOAN
 VALUE COST
 PAR VALUE
 VALUE PAR
 VALUE
 PORTFOLIOS

 Restructured
 \$ 9 \$ 5
 55.6% \$ 6

66.7% --%
 Problem 237
 14 5.9 14
 5.9 --
 Potential
 problem 277
 218 78.7
 172 62.1
 0.3 -----

 -- -----
 Total net
 carrying
 value \$ 523
 \$ 237 45.3
 \$ 192 36.7
 0.3% =====
 =====
 =====
 Cumulative
 write-
 downs
 recognized
 (2) \$ 261
 =====

-
- (1) The difference between par value and amortized cost of \$1.43 billion at December 31, 2008 is primarily attributable to write-downs. Par value has been reduced by principal payments.
 - (2) Cumulative write-downs recognized only reflects impairment write-downs related to investments within the problem, potential problem and restructured categories.

At December 31, 2008, amortized cost for the problem category was \$188 million and was comprised of \$80 million of corporates (primarily privately placed), \$48 million of financial sector-related holdings, \$19 million of real estate investment trusts and \$9 million of bank loans. Also included were \$18 million of market value CDO, \$10 million of ABS CDO, \$3 million of ABS RMBS, and \$1 million of Alt-A. The increase over December 31, 2007 is attributable to the addition of fixed income and bank loan holdings that either are in default with respect to principal or interest and/or are investments issued by companies that went into bankruptcy during the period. The amortized cost of problem investments with a fair value less than 70% of amortized cost totaled \$64 million, with unrealized losses of \$29 million and fair value of \$35 million.

At December 31, 2008, amortized cost for the potential problem category was \$432 million and was comprised of \$130 million of other CDO, \$79 million of Alt-A, \$48 million of ABS RMBS and \$13 million of other ABS. Also included were \$65 million of corporates (primarily privately placed home builders and suppliers), \$41 million of financial sector-related holdings, \$37 million of foreign government holdings, \$13 million of bank loans and \$6 million of CRE CDO. The increase over December 31, 2007 is primarily attributable to the additions of certain real estate-related holdings, including securities collateralized by residential and commercial mortgage loans, as well as market value, cash flow and synthetic CDO. Also contributing to the increase were financial sector-related holdings and corporates, primarily privately placed. The amortized cost of potential problem investments with a fair value less than 70% of amortized cost totaled \$194 million, with unrealized losses of \$127 million and fair value of \$67 million.

We evaluated each of these investments through our portfolio monitoring process at December 31, 2008 and recorded write-downs when appropriate. We further concluded that any remaining unrealized losses on these investments were temporary in nature and that we have the intent and ability to hold the securities until recovery.

NET INVESTMENT INCOME The following table presents net investment income for the years ended December 31.

(\$ IN
 MILLIONS)
 2008 2007
 2006 -----

Fixed	
income	
securities	
\$ 3,112	\$
3,589	\$
3,505	
Mortgage	
loans	580
552	508
Equity	
securities	
7	4
2	
Limited	
partnership	
interests	
29	87
42	
Other	121
243	257
--	--
-----	-----
-----	-----
Investment	
income,	
before	
expense	
3,849	
4,475	
4,314	
Investment	
expense	
(129)	
(270)	
(257)	----
-----	-----
-----	-----
Net	
investment	
income (1)	
\$ 3,720	\$
4,205	\$
4,057	
=====	
=====	
=====	

(1) Beginning in the fourth quarter of 2008, income from EMA LP is reported in realized capital gains and losses. EMA LP income for periods prior to the fourth quarter of 2008 is reported in net investment income. The amount of EMA LP income included in net investment income was \$14 million in 2008, \$50 million in 2007 and \$15 million in 2006. The amount of EMA LP loss included in realized capital gains and losses was \$14 million in 2008.

Total investment expenses decreased \$141 million in 2008 compared to 2007, after increasing \$13 million in 2007 compared to 2006. The 2008 decrease was primarily due to lower expenses associated with a lower amount of collateral received in connection with securities lending transactions. The average amount of collateral held in connection with securities lending was approximately \$1.65 billion in 2008 compared to approximately \$2.79 billion in 2007, as a result of actions to reduce our securities lending balances.

NET REALIZED CAPITAL GAINS AND LOSSES The following table presents the components of realized capital gains and losses and the related tax effect for the years ended December 31.

(\$ IN	
MILLIONS)	
2008	2007
2006	-----
-----	-----
-----	-----
-----	-----
Sales (1)	
\$ 184	\$ 70
\$ (29)	
Impairment	
write-	
downs (2)	

(1,227)
(118) (21)
Change in
intent
write-
downs (1)
(3)
(1,207)
(92) (60)
Valuation
of
derivative
instruments
(985) (63)
(17) EMA
LP income
(4) (14) -
- -
Settlement
of
derivative
instruments
197 6 48 -

Realized
capital
gains and
losses,
pre-tax
(3,052)
(197) (79)
Income tax
benefit
1,067 69
28 -----

Realized
capital
gains and
losses,
after-tax
\$ (1,985)
\$ (128) \$
(51)
=====

-
- (1) To conform to the current period presentation, certain amounts in the prior periods have been reclassified.
 - (2) Impairment write-downs reflect issue specific other-than-temporary declines in fair value, including instances where we could not reasonably assert that the recovery period would be temporary.
 - (3) Change in intent write-downs reflect instances where we cannot assert a positive intent to hold until recovery.
 - (4) Beginning in the fourth quarter of 2008, income from EMA LP is reported in realized capital gains and losses. EMA LP income for periods prior to the fourth quarter of 2008 is reported in net investment income.

SALES net realized gains in 2008 were primarily due to net realized gains on fixed income securities of \$239 million comprised of gross gains of \$626 million and gross losses of \$387 million. The net realized gains on sales in 2007 were primarily due to net realized gains on limited partnership interests of \$44 million comprised of gross gains of \$45 million and gross losses of \$1 million.

The ten largest losses from sales of individual securities for the year ended December 31, 2008 totaled \$77 million and ranged from \$4 million to \$15 million. One security totaling \$11 million was in an unrealized loss position greater than or equal to 20% of amortized cost for fixed income securities or cost for equity securities for a period of less than six consecutive months. Two securities totaling \$18 million were in an unrealized loss position greater than or equal to 20% of amortized cost for fixed income securities or cost for equity

securities for a period of more than six but less than twelve consecutive months.

Our largest aggregate loss on sales and write-downs are shown in the following table by issuer and its affiliates. No other issuer together with its affiliates had an aggregated loss on sales and write-downs greater than 1.2% of the total gross loss on sales and write-downs on fixed income and equity securities.

FAIR VALUE
GAIN/
DECEMBER 31,
NET AT SALES
LOSS ON
WRITE- 2008
UNREALIZED
(\$ IN
MILLIONS)
("PROCEEDS")
SALES DOWNS
HOLDINGS (1)
GAIN (LOSS)

-- -----

---- Finance
company \$
136 \$ (6) \$
(69) \$ 6 \$ -
- Savings
and loan 17
-- (72) -- -
- Synthetic
CDO -- --
(50) 14 (10)
Savings and
loan -- --
(45) -- --
Large
international
insurer 68 1
(38) 38 (7)
Residential
mortgage
investor --
-- (35) 6
(2) UK
homebuilder
-- -- (34)
22 -- Door
and window
manufacturer
-- -- (31)
37 7 Private
equity
property
fund 8 --
(31) -- -- -

--- Total \$
229 \$ (5) \$
(405) \$ 123
\$ (12)
=====
=====
=====
=====
=====

(1) Holdings include fixed income securities at amortized cost or equity securities at cost.

The circumstances of the above losses are considered to be security or

issue specific and are not expected to have a material effect on other holdings in our portfolio.

We may sell or change our intent to hold a security until recovery for impaired fixed income or equity securities that were in an unrealized loss position at the previous reporting date, or other investments where the fair value has declined below the amortized cost or cost, in situations where significant unanticipated new facts and circumstances emerge or existing facts and circumstances increase in significance and are anticipated to adversely impact a security's future valuations more than previously expected; including negative developments that would change the view of long term investors and their intent to continue to hold the investment, subsequent credit deterioration of an issuer or holding, subsequent further deterioration in capital markets (i.e. debt and equity) and of economic conditions, subsequent further deterioration in the financial services and real estate industries, liquidity needs, unanticipated federal income tax situations involving capital gains and capital loss carrybacks and carryforwards with specific expiration dates, investment risk mitigation actions, and other new facts and circumstances that would cause a change in our previous intent to hold a security to recovery or maturity.

Upon approval of programs involving the expected disposition of investments, portfolio managers identify a population of suitable investments, typically larger than needed to accomplish the objective, from which specific securities are selected to sell. Due to our change in intent to hold until recovery, we recognize impairments on investments within the population that are in an unrealized loss position. Further unrealized loss positions that develop subsequent to the original write-down are recognized in the reporting period in which they occur through the date the program is closed. The program is closed when the objectives of the program are accomplished or a decision is made not to fully complete it, at which time an evaluation is performed of any remaining securities and where appropriate they are redesignated as having the intent to hold to recovery. Reasons resulting in a decision not to complete an approved program include matters such as the mitigation of concerns that led to the initial decision, changes in priorities or new complications that emerge from significant unanticipated developments, such as subsequent significant deterioration which we view to be temporary in nature, to the point at which securities could only be sold at prices below our view of their intrinsic values, or subsequent favorable developments that support a return to having the intent to hold to recovery. Subsequent other-than-temporary impairment evaluations utilize the amortized cost or cost basis that reflect the write-downs. Fixed income securities subject to change in intent write-downs, including those redesignated as intent to hold, continue to earn investment income and any discount or premium from the amortized cost basis that reflects the write-downs is recognized using the effective yield method over the expected life of the security.

As previously described above, it is not possible to reliably identify a reasonably likely circumstance that would result in a change in intent to hold securities to recovery leading to the reporting of additional realized capital losses, since they result from significant unanticipated changes. Our fixed income securities and equity securities have gross unrealized losses of \$8.61 billion and \$25 million, respectively, at December 31, 2008 that we concluded were temporary in nature and we have the intent and ability to hold the securities until recovery.

IMPAIRMENT WRITE-DOWNS for the years ended December 31 are presented in the following table.

(\$ IN
MILLIONS)
2008 2007
2006 -----

Fixed
income
securities
\$ (1,123)
\$ (104) \$
(14)
Equity
securities
(7) -- (2)
Limited
partnership
interests

(66) (10)
 -- Short-term
 investments
 -- (1) (3)
 Other
 investments
 (31) (3)
 (2) -----

 --- Total
 impairment
 write-downs \$
 (1,227) \$
 (118) \$
 (21)
 =====
 =====
 =====

\$803 million or 71.5% of the fixed income security write-downs in 2008 related to impaired securities that were performing in line with anticipated or contractual cash flows, but which were written down primarily because of expected deterioration in the performance of the underlying collateral or our assessment of the probability of future default. As of December 31, 2008, for these securities, there have been no defaults or defaults impacting classes lower in the capital structure. \$92 million of the fixed income security write-downs in 2008 primarily related to securities experiencing a significant departure from anticipated cash flows; however, we believe they retain economic value and \$105 million related to securities for which future cash flows are very uncertain. Equity securities were written down primarily due to the length of time and extent fair value was below cost, considering our assessment of the financial condition, near-term and long-term prospects of the issuer, including relevant industry conditions and trends.

Impairment write-downs and cash received, inclusive of sales, on these investments for the year ended December 31, 2008 are presented in the following table. Notwithstanding our intent and ability to hold these securities with impairment write-downs, we concluded that we could not reasonably assert that the recovery period would be temporary.

(\$ IN MILLIONS)
 DECEMBER 31, 2008

PERFORMING IN
 ACCORDANCE WITH
 ANTICIPATED OR
 IMPAIRMENT CASH
 CONTRACTUAL CASH
 FLOWS WRITE-DOWNS
 RECEIVED(3) -----

----- Alt-A No
 defaults in
 underlying
 collateral \$ (30)
 \$ 15 Defaults
 lower in capital
 structure (14) 9

 (44) 24 ABS RMBS
 (142) 13 ABS CDO
 (63) 5 CMBS and
 CRE CDO (46) 6
 Other CDO (88) 14
 Synthetic CDO
 (186) 8 Corporate
 Automotive (2) 4
 Bond reinsurer -
 convertible to
 perpetual
 security (22) 1
 Financials (69) 6

Gaming (3) --
 Home construction
 (64) 8 Oil and
 gas (2) 1
 Publishing (4) --
 Real estate and
 Real Estate
 Investment Trust
 (43) 3
 Telecommunications
 (10) -- -----

 ---- Subtotal
 (219) 23 Other
 (15) 13 -----

 ---- SUBTOTAL (1)
 (803) 106
 DEPARTURE FROM
 ANTICIPATED OR
 CONTRACTUAL CASH
 FLOWS Future cash
 flows expected -
 ABS RMBS (23) 6
 Corporate
 Broadcasting (23)
 1 Equity
 structured note
 (30) --
 Financials (16) 8
 ----- -

 SUBTOTAL (2) (92)
 15 Future cash
 flows very
 uncertain - Other
 CDO (33) 1 ABS
 RMBS (4) 1
 Corporate Food
 manufacturer (10)
 -- Financials
 (58) 9 -----

 --- SUBTOTAL
 (105) 11
 Investments
 disposed (123)
 106 -----

 TOTAL FIXED
 INCOME SECURITIES
 (4) \$ (1,123) (4)
 \$ 238
 =====
 =====
 TOTAL EQUITY
 SECURITIES \$ (7)
 \$ 14
 =====
 =====
 TOTAL LIMITED
 PARTNERSHIP
 INTERESTS \$ (66)
 \$ 13
 =====
 =====
 TOTAL OTHER
 INVESTMENTS \$
 (31) \$ 6
 =====
 =====

 (1) Written down primarily because of expected deterioration in the performance of the underlying collateral or our assessment of the probability of future default. As of December 31, 2008, for the securities with direct interest in the lender, there have been no defaults. For securities supported by collateral, there have been no defaults or defaults have occurred in classes lower in the capital

- structure.
- (2) Experienced a significant departure from anticipated residual cash flows. While these fixed income security write-downs were valued at a significant discount to cost, we believe these securities retain economic value.
 - (3) Cash received includes both income and principal collected during the period and proceeds upon sale.
 - (4) Impairment write-downs on our illiquid portfolios were \$654 million.

CHANGE IN INTENT WRITE-DOWNS totaling \$1.21 billion in 2008 included \$1.12 billion for fixed income securities, \$14 million for equity securities and \$73 million for mortgage loans compared to \$64 million for fixed income securities and \$28 million for mortgage loans in 2007. The change in intent write-downs in 2008 were a result of our risk mitigation and return optimization programs and ongoing comprehensive reviews of our portfolios.

Change in intent write-downs for the year ended December 31, 2008 are presented in the table below.

FAIR VALUE OF
(\$ IN
MILLIONS)
OUTSTANDING
SFAS NO. 157
CHANGE IN
INTENT NET
REALIZED
CRITERIA
SECURITY TYPE
LEVEL ASSETS
CAPITAL LOSS
(3) - -----

- RISK
MITIGATION
Targeted
reductions
(1) in
commercial
real CRE CDO
3 \$ 27 \$
(330) estate
exposure
where it is
anticipated
that future
downside risk
remains.
Considerations
CMBS 2 --
(22) included
position held
in the
capital
structure, 3
29 (203)
vintage year,
illiquidity
and
deteriorating
fundamentals.
Mortgage
loans 3 127
(71) Targeted
reductions
(1) in
residential
real estate
where
management
believes
there is a
risk Prime 2
-- (6) of

future
 material
 declines in
 price in the
 3 -- (5)
 event of
 continued
 deterioration
 in the
 economy.
 Considerations
 included
 position held
 Alt-A 3 20
 (44) in the
 capital
 structure,
 projected
 performance
 of the
 collateral,
 and expected
 internal
 rates ABS
 RMBS 3 33
 (200) of
 return.
 Targeted
 reductions
 (1) in
 financial
 sector
 Financial
 sector 2 14
 (154)
 exposure
 included
 securities
 issued by
 certain 3 --
 (29) regional
 banks and
 certain large
 financial
 institutions.
 Other 2 4
 (18) -----

 Total risk
 mitigation
 254 (1,082)
 Individual
 identification
 520 (116)
 Other -- (9)

 ----- Total \$
 774 \$ (1,207)
 (2) =====
 =====

-
- (1) Targeted reductions are made from identified specific investments.
 - (2) Change in intent write-downs on our illiquid portfolios were \$811 million.
 - (3) Change in intent write-downs are related to the risk mitigation targeted reduction for this security type for the year and not for the outstanding change in intent assets at December 31, 2008.

Investments for which we had changed our intent to hold to recovery as of June 30, 2008 totaled \$2.97 billion and included \$2.64 billion as part of the risk mitigation and return optimization programs and \$329 million related to individual securities. The following table summarizes the activity related to investments for which we had changed our intent to hold.

(\$ IN
MILLIONS)

Carrying
value as of
June 30,
2008 \$
2,966 Re-
designated
as intent
to hold to
recovery as
of October
1, 2008 (1)
(834)
Sales: Risk
mitigation
and return
optimization
program (2)
(1,029)
Other
programs
(231) Net
realized
capital
gains and
losses on
sales: Risk
mitigation
and return
optimization
program (2)
(72) Other
programs
(8)
Additional
change in
intent
designations
(3) 516
Write-downs
(4) (552)
Other 18 --

Carrying
value as of
December
31, 2008 \$
774
=====

-
- (1) Net unrealized capital losses on these re-designated investments were \$202 million as of December 31, 2008.
 - (2) Net proceeds from the sales of risk mitigation and return optimization actions totaled \$1.03 billion with an additional loss of \$72 million or 93% of fair values reported at June 30, 2008.
 - (3) Comprised \$275 million and \$241 million for which we changed our intent to hold in the third and fourth quarter of 2008, respectively, due to unanticipated changes in facts and circumstances.
 - (4) Includes change in intent write-downs of \$262 million and \$191 million in the third and fourth quarter of 2008, respectively, and impairment write-downs of \$91 million and \$8 million in the third and fourth quarter of 2008, respectively.

Our original objective in our June 30, 2008 risk mitigation and return optimization program was to reduce our exposure to the identified investments in an orderly fashion prior to additional significant negative impacts. Though we were able to complete a considerable portion of the reduction, approximately \$1.03 billion of this program, during the third and fourth quarters of 2008 the financial markets experienced additional and severe dislocation. A series of events, which includes the effects of failures of large financial institutions and intermediaries and various intervention by the government, significantly increased the level of uncertainty in the market. These conditions drove significant volatility in the levels of liquidity and put additional and immediate downward pressures on prices of certain of these investments in respect to our estimated intrinsic values. As a result of these market conditions, which have worsened, we determined that we would not be able to sell certain of these investments at our view of their intrinsic values.

exceeded amortized cost by \$17 million at December 31, 2008. Valuation gains and losses are converted into cash for securities with embedded options upon our election to sell these securities. In the event the economic value of the options is not realized, we will recover the par value if held to maturity unless the issuer of the note defaults. Total par value exceeded fair value by \$206 million at December 31, 2008.

Losses on derivatives used for interest rate risk management but which have not been designated as accounting hedges, primarily in our duration management programs, were related to changing interest rates.

A changing interest rate environment will drive changes in our portfolio duration targets at a tactical level. A duration target and range is established with an economic view of liabilities relative to a long-term investment portfolio view. Tactical duration management is accomplished through both cash market transactions including new purchases and derivative activities that generate realized gains and losses. As a component of our approach to managing portfolio duration, realized gains and losses on certain derivative instruments are most appropriately considered in conjunction with the unrealized gains and losses on the fixed income portfolio. This approach mitigates the impacts of general interest rate changes to the overall financial condition of the Company.

The table below presents the realized capital gains and losses (pre-tax) on the valuation and settlement of derivative instruments shown by underlying exposure and derivative strategy for the years ended December 31.

(\$ IN MILLIONS)

2008 2007 2006
2008

EXPLANATIONS --

VALUATION
SETTLEMENTS
TOTAL TOTAL
TOTAL -----

----- RISK
REDUCTION
Duration gap
management \$
(543) \$ 40 \$
(503) \$ (27) \$
(51) Interest
rate caps,
floors and
swaps are used
to align
interest-rate
sensitivities
of our assets
and
liabilities.
The contracts
settle based on
differences
between current
market rates
and a
contractually
specified fixed
rate through
expiration. The
contracts can
be terminated
and settled at
anytime with a
minimal
additional
cost. The
maximum loss on
caps and floors

would be limited to the amount of premium paid for the protection. The change in valuation reflects the changing value of expected future settlements from changing interest rates, which may vary over the period of the contracts. The 2008 year to date ("YTD") losses, resulting from decreasing interest rates, are offset in unrealized gains in OCI to the extent it relates to changes in risk-free rates; however, the impact of widening credit spreads more than offset this benefit. Anticipatory hedging (1) 154 153 (30) 17 Futures are used to protect investment spread from interest rate changes for mismatches in the timing of cash flows between product sales and the related investment activity. The futures contracts are exchange traded, daily cash settled and can be exited at any time for minimal additional cost. If the cash flow mismatches are such that a positive net investment position is being hedged, there is an offset for the related investments unrealized loss in OCI. The 2008 YTD amounts reflect

decreases in
risk-free
interest rates
on a net long
position as
liability
issuances
exceeded asset
acquisitions.
Hedging of
interest Value
of expected
future
settlements and
the rate
exposure in
associated
value of future
credited
interest,
annuity
contracts (22)
(7) (29) (22) 1
which is
reportable in
future periods
when incurred,
decreased due
to declining
interest
Hedging
unrealized
rates. gains on
equity indexed
notes -- 7 7 --
-- Hedge
ineffectiveness
(2) (2) (4)
(13) (7) The
hedge
ineffectiveness
of (\$2 million)
includes \$416
million in
realized
capital losses
on swaps that
were offset by
\$414 million in
realized
capital gains
on the hedged
risk. Foreign
currency
contracts --
(1) (1) (13)
(5) Credit risk
reduction 20
(3) 17 -- --
Valuation gain
is the results
of widening
credit spreads
on referenced
credit
entities. Other
1 -- 1 -- -- --

TOTAL RISK
REDUCTION \$
(547) \$ 188 \$
(359) \$ (105) \$
(45) INCOME
GENERATION
Asset
replication -
Credit default
swaps are used
to replicate

fixed credit
exposure \$ (71)
\$ 9 \$ (62) \$
(18) \$ 4 income
securities and
to complement
the cash market
when credit
exposure to
certain issuers
is not
available or
when the
derivative
alternative is
less expensive
than the cash
market
alternative.

The credit
default swaps
typically have
five year term
for which we
receive
periodic
premiums
through
expiration. The
2008 YTD
changes in
valuation are
due to the
widening credit
spreads, and
would only be
converted to
cash upon
disposition
which can be
done at any
time, or if the
credit event
specified in
the contract
occurs. The
maximum
exposure is
equal to the
notional amount
of the credit
derivative. If
the credit
event specified
in the contract
occurs, we are
obligated to
pay the
counterparty
the notional
amount of the
contract and
receive in
return the
referenced
defaulted
security or
similar
security. As of
December 31,
2008, we had
\$517 million of
notional
outstanding. --

TOTAL INCOME
GENERATION \$
(71) \$ 9 \$ (62)
\$ (18) \$ 4 ----

the event the economic value of the options is not realized, we will recover the par value of the host fixed income security if held to maturity unless the issuer of the note defaults. Par value exceeded fair value by \$167 million at December 31, 2008. Equity-indexed notes are subject to our comprehensive portfolio monitoring and watchlist processes to identify and evaluate when the carrying value may be other-than-temporarily impaired. The following table compares the December 31, 2008 and December 31, 2007 holdings, respectively.

(\$ in millions)

December 31, 2007	December 31, 2008	CHANGE
-----	-----	-----
Par value \$ 800	\$ 800	
=====	=====	=====
-----	-----	-----
Amortized cost of host contract \$ 486	\$(11)	\$ 497
Fair value of equity-indexed call option	132	(290)
-----	-----	-----
- Total amortized cost	\$ 618	\$(301)
-----	-----	-----
=====	=====	=====
-----	-----	-----
Total fair value	\$ 633	\$(291)
-----	-----	-----
-----	-----	-----
Unrealized gain/ loss	\$ 924	
-----	-----	-----

15 \$ 10 \$ 5
Conversion
options in
fixed income
Convertible
bonds are
fixed income
securities
that
securities
(77) -- (77)

28 37 contain
embedded
options.

Changes in
valuation of
the embedded
option are
reported in
realized

capital gains
and losses.

The results
generally
track the
performance
of underlying
equities.

Valuation
gains and
losses are
converted
into cash
upon our
election to
sell these
securities.

In the event
the economic
value of the
options is
not realized,
we will

recover the
par value of
the host
fixed income
security if
held to
maturity

unless the
issuer of the
note

defaults. Par
value

exceeded fair
value by \$39
million at
December 31,
2008.

Convertible
bonds are
subject to
our

comprehensive
portfolio
monitoring

and watchlist
processes to
identify and
evaluate when

the carrying
value may be
other-than-
temporarily

impaired. As
a result of
this process,
four issues

were written-
down during

2008. The following table compares the December 31, 2008 and December 31, 2007 holdings, respectively.

Change December Change due to December (\$ in millions) 31, in Fair Net Sale 31, 2008 Value Activity 2007

-----	-----	-----
Par value \$		
378 \$ --		
\$(181) \$ 559		
=====	=====	
Amortized cost of host contract \$		
247 \$ 7		
\$(147) \$ 387		
Fair value of conversion option 90		
(77) (23) 190		
-----	-----	-----
Total amortized cost \$ 337		
\$(70) \$(170)		
\$ 577 =====		
===== Total fair value \$		
339 \$(88)		
\$(153) \$ 580		
=====	=====	
Unrealized \$		
2 \$(18) \$ 17		
\$ 3 gain/loss		
-----	-----	-----
-----	-----	-----
TOTAL ACCOUNTING \$		
(367) \$ -- \$		
(367) \$ 66 \$		
72 -----		
-----	-----	-----
TOTAL \$ (985)		
\$ 197 \$ (788)		
\$ (57) \$ 31		
=====	=====	
=====	=====	
=====	=====	
=====	=====	

Included in the table above are net realized capital gains on the valuation and settlement of derivative instruments related to credit spread risk hedging from our risk mitigation and return optimization programs initiated in 2008 totaling \$7 million for the year ended December 31, 2008.

FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The following table provides additional details regarding Level 1, 2 and 3 financial assets and financial liabilities by their classification in the Consolidated Statement of Financial Position at December 31, 2008. For further discussion of Level 1, 2 and 3 financial assets and financial liabilities, see Note 2 of the consolidated financial statements and the Application of Critical Accounting Estimates section of the MD&A.

(\$ IN
MILLIONS)
QUOTED PRICES
IN ACTIVE
SIGNIFICANT
MARKETS FOR
OTHER
SIGNIFICANT
IDENTICAL
OBSERVABLE
UNOBSERVABLE
OTHER BALANCE
AS OF ASSETS
INPUTS INPUTS
VALUATIONS
DECEMBER 31,
(LEVEL 1)
(LEVEL 2)
(LEVEL 3) AND
NETTING 2008

- -----
- -----

FINANCIAL
ASSETS Fixed
income
securities:
Corporate \$ -
- \$ 11,460 \$
449 \$ 11,909
Corporate
privately
placed
securities --
2,942 9,418
12,360
Municipal --
2,605 50
2,655
Municipal -
ARS -- -- 653
653 U.S.
government
and agencies
276 3,411 --
3,687 ABS
RMBS -- --
1,248 1,248
Alt-A -- --
315 315 Other
CD0 -- -- 752
752 Other ABS
-- -- 402 402
ABS CD0 -- --
6 6 CRE CD0 -
- -- 27 27
CMBS -- 3,320
383 3,703
Preferred
stock -- 9 1
10 MBS --
2,162 242
2,404 Foreign
government --
2,100 --
2,100 ABS -
Credit card,
auto and
student loans

 --- TOTAL
 INVESTMENTS
 619 32,212
 14,417 12,524
 59,772 -----

 Separate
 account
 assets 8,239
 -- -- --
 8,239 Other
 assets (1) --
 1 -- -- -----

 - TOTAL
 FINANCIAL
 ASSETS \$
 8,857 \$
 32,212 \$
 14,418 \$
 12,524 \$
 68,011
 =====
 =====
 =====
 =====

% of total
 financial
 assets 13.0%
 47.4% 21.2%
 18.4% 100.0%

FINANCIAL
 LIABILITIES
 Contractholder
 funds:
 Derivatives
 embedded in
 annuity
 contracts \$ -
 - \$ (37) \$
 (265) \$ (302)
 Other
 liabilities:
 Free-standing
 derivatives -
 - (1,118)
 (106) (1,224)
 Non-recurring
 basis -- -- -
 - --
 Counterparty
 and cash
 collateral
 netting (1) \$
 460 460 -----

 - TOTAL
 FINANCIAL
 LIABILITIES \$
 -- \$ (1,155)
 \$ (371) \$ 460
 \$ (1,066)
 =====
 =====
 =====

```

=====
=====
% of total
financial
liabilities -
-% 108.4%
34.8% (43.2)%
100.0%

```

(1) In accordance with Financial Accounting Standards Board ("FASB") Staff Position No. FIN 39-1, AMENDMENT OF FASB INTERPRETATION NO. 39, we net all fair value amounts recognized for derivative instruments and fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral executed with the same counterparty under a master netting agreement. At December 31, 2008, the right to reclaim cash collateral was offset by securities held, and the obligation to return collateral was \$20 million.

The following table provides a summary of changes in fair value during the year ended December 31, 2008 of Level 3 financial assets and financial liabilities held at fair value on a recurring basis at December 31, 2008.

```

TOTAL REALIZED
AND UNREALIZED
GAINS (LOSSES)
INCLUDED IN: ---
-----
OCI ON
PURCHASES,
BALANCE AS OF
STATEMENT OF
SALES, ISSUANCES
JANUARY 1,
FINANCIAL AND
SETTLEMENTS, ($
IN MILLIONS)
2008 NET INCOME
(1) POSITION NET
-----
-----
- FINANCIAL
ASSETS Fixed
income
securities:
Corporate $ 747
$ (94) $ (50) $
(354) Corporate
privately placed
securities
11,098 (226)
(1,097) (665)
Municipal 68 --
(7) 48 Municipal
- ARS 163 --
(65) (60) ABS
RMBS 2,382 (351)
(409) (374) Alt-
A 588 (92) (90)
(91) Other CDO
1,961 (305)
(854) (30) Other
ABS 720 (23)
(109) (239) ABS
CDO 36 (63) 37
(4) CRE CDO 566
(415) 161 (285)
CMBS 224 (38)
(473) (106)
Preferred stock
-- 1 -- -- MBS
28 (1) (49) (22)
Foreign
government -- --

```

-- (5) ABS -
 Credit card,
 auto and student
 loans 249 (10)
 (24) (135) -----

 ----- Total
 fixed income
 securities
 18,830 (1,617)
 (3,029) (2,322)
 Equity
 securities 61
 (3) (12) 20
 Other
 investments:
 Free-standing
 derivatives, net
 (6) (125) -- 38

TOTAL
 INVESTMENTS
 18,885 (1,745)
 (3,041) (2,264)
 Other assets 2
 (1) -- -- -----

----- TOTAL
 RECURRING LEVEL
 3 FINANCIAL
 ASSETS \$ 18,887
 \$ (1,746) \$
 (3,041) \$
 (2,264)
 =====
 =====
 =====

=====

FINANCIAL
 LIABILITIES
 Contractholder
 funds:
 Derivatives
 embedded in
 annuity
 contracts \$ 4 \$
 (270) \$ -- \$ 1 -

TOTAL RECURRING
 LEVEL 3
 FINANCIAL
 LIABILITIES \$ 4
 \$ (270) \$ -- \$ 1
 =====
 =====
 =====

=====

TOTAL GAINS
 (LOSSES)
 INCLUDED IN NET
 INCOME FOR NET
 INSTRUMENTS
 TRANSFERS IN
 BALANCE AS OF
 STILL HELD AT
 AND/OR (OUT)
 DECEMBER 31,
 DECEMBER 31, (\$
 IN MILLIONS) OF
 LEVEL 3 2008
 2008 (4) -----

----- FINANCIAL
ASSETS Fixed
income
securities:
Corporate \$ 200
\$ 449 \$ (102)
Corporate
privately placed
securities 308
9,418 (265)
Municipal (59)
50 -- Municipal
- ARS 615 653 --
ABS RMBS --
1,248 (330) Alt-
A -- 315 (71)
Other CDO (20)
752 (307) Other
ABS 53 402 (10)
ABS CDO -- 6
(63) CRE CDO --
27 (179) CMBS
776 383 (13)
Preferred stock
-- 1 -- MBS 286
242 -- Foreign
government 5 --
-- ABS - Credit
card, auto and
student loans
107 187 -- -----

----- Total
fixed income
securities 2,271
14,133 (1,340)
Equity
securities (39)
27 (3) Other
investments:
Free-standing
derivatives, net
-- (93) (2) (37)

TOTAL
INVESTMENTS
2,232 14,067 (3)
(1,380) Other
assets -- 1 (1)

TOTAL RECURRING
LEVEL 3
FINANCIAL ASSETS
\$ 2,232 \$ 14,068
\$ (1,381)
=====

=====

FINANCIAL
LIABILITIES
Contractholder
funds:
Derivatives
embedded in
annuity
contracts \$ -- \$
(265) \$ (270) --

----- TOTAL
RECURRING LEVEL
3 FINANCIAL
LIABILITIES \$ --
\$ (265) \$ (270)

90.1	ABS
RMBS	1,248
53.3	62.4
Alt-A	315
61.4	72.9
Other	CD0
752	33.8
40.5	Other
ABS	402 62.0
75.6	ABS CD0
6	4.4 60.0
CRE	CD0 27
13.4	108.0
CMBS	383
30.8	33.2
Preferred	stock 1
100.0	100.0
MBS	242 71.2
72.2	ABS -
Credit card,	auto and
student	loans 187
80.6	86.2 --

Total fixed	income
securities	
14,133	70.0
77.8	-----
----	Equity
securities:	
U.S.	
equities	15
N/A	100.0
International	
equities	11
137.5	78.6
Other	1 33.3
100.0	-----
-----	Total
equity	
securities	
27	N/A 90.0

Other	
investments:	
Free-	
standing	
derivatives	
13	N/A N/A -

Total other	
investments	
13	N/A N/A -

Sub-total	
recurring	
Level 3	
investments	
14,173	70.1
77.9	Non-
recurring	
basis	244
N/A	100.0 --

TOTAL LEVEL	
3	
INVESTMENTS	
\$	14,417
71.3	78.1
=====	

Non-recurring investments include certain mortgage loans, limited partnership interests and other investments remeasured at fair value due to our change in intent write-downs and other-than-temporary impairments at December 31, 2008.

MARKET RISK

Market risk is the risk that we will incur losses due to adverse changes in equity, interest, credit spreads, or currency exchange rates and prices. Adverse changes to these rates and prices may occur due to changes in the liquidity of a market or market segment, insolvency or financial distress of key market makers or participants or changes in market perceptions of credit worthiness and/or risk tolerance. Our primary market risk exposures are to changes in interest rates, credit spreads and equity prices, although we also have a smaller exposure to changes in foreign currency exchange rates.

The active management of market risk is integral to our results of operations. We may use the following approaches to manage exposure to market risk within defined tolerance ranges: 1) rebalancing existing asset or liability portfolios, 2) changing the character of investments purchased in the future and 3) using derivative instruments to modify the market risk characteristics of existing assets and liabilities or assets expected to be purchased. For a more detailed discussion of our use of derivative financial instruments, see Note 7 of the consolidated financial statements.

OVERVIEW In formulating and implementing guidelines for investing funds, we seek to earn returns that enhance our ability to offer competitive rates and prices to customers while contributing to attractive and stable profits and long-term capital growth. Accordingly, our investment decisions and objectives are a function of the underlying risks and our product profiles.

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Investment policies define the overall framework for managing market and other investment risks, including accountability and controls over risk management activities. These investment policies, which have been approved by our board of directors, specify the investment limits and strategies that are appropriate given our liquidity, surplus, product profile and regulatory requirements. Executive oversight of investment activities is conducted primarily through our board of directors and investment committee. Asset-liability management ("ALM") policies further define the overall framework for managing market and investment risks. ALM focuses on strategies to enhance yields, mitigate market risks and optimize capital to improve profitability and returns. ALM activities follow asset-liability policies that have been approved by our board of directors. These ALM policies specify limits, ranges and/or targets for investments that best meet our business objectives in light of our product liabilities.

We manage our exposure to market risk through the use of asset allocation, duration and value-at-risk limits, simulation, and as appropriate, through the use of stress tests. We have asset allocation limits that place restrictions on the total funds that may be invested within an asset class. We have duration limits on our investment portfolio and, as appropriate, on individual components of the portfolio. These duration limits place restrictions on the amount of interest rate risk that may be taken. Our value-at-risk limits are intended to restrict the potential loss in fair value that could arise from adverse movements in the fixed income, equity, and currency markets based on historical volatilities and correlations among market risk factors. Comprehensive day-to-day management of market risk within defined tolerance ranges occurs as portfolio managers buy and sell within their respective markets based upon the acceptable boundaries established by investment policies. This day-to-day management is integrated with and informed by the activities of the ALM organization. This integration is intended to result in a prudent, methodical and effective adjudication of market risk and return, conditioned by the unique demands and dynamics of our product liabilities and supported by the continuous application of advanced risk technology and analytics.

INTEREST RATE RISK is the risk that we will incur a loss due to adverse changes in interest rates relative to the interest rate characteristics of interest bearing assets and liabilities. This risk arises from many of our primary activities, as we invest substantial funds in interest-sensitive assets and issue interest-sensitive liabilities. Interest rate risk includes risks related to changes in U.S. Treasury yields and other key risk-free reference yields.

We manage the interest rate risk in our assets relative to the interest rate risk in our liabilities. One of the measures used to quantify this exposure is duration. Duration measures the price sensitivity of the assets and liabilities to changes in interest rates. For example, if interest rates increase 100 basis points, the fair value of an asset with a duration of 5 is expected to decrease in value by approximately 5%. At December 31, 2008, the difference between our asset and liability duration was approximately 0.61, compared to a 0.63 gap at December 31, 2007. A positive duration gap indicates that the fair value of our assets is more sensitive to interest rate movements than the fair value of our liabilities.

We seek to invest premiums, contract charges and deposits to generate

future cash flows that will fund future claims, benefits and expenses, and that will earn stable spreads across a wide variety of interest rate and economic scenarios. To achieve this objective and limit interest rate risk, we adhere to a philosophy of managing the duration of assets and related liabilities within predetermined tolerance levels. This philosophy is executed using duration targets for fixed income investments in addition to interest rate swaps, futures, forwards, caps, floors and swaptions to reduce the interest rate risk resulting from mismatches between existing assets and liabilities, and financial futures and other derivative instruments to hedge the interest rate risk of anticipated purchases and sales of investments and product sales to customers.

We pledge and receive collateral on certain types of derivative contracts. For futures and option contracts traded on exchanges, we have pledged securities as margin deposits totaling \$28 million as of December 31, 2008. For OTC derivative transactions including interest rate swaps, foreign currency swaps, interest rate caps, interest rate floors, and credit default swaps, master netting agreements are used. These agreements allow us to net payments due for transactions covered by the agreements and, when applicable, we are required to post collateral. As of December 31, 2008, we held cash of \$20 million pledged by counterparties as collateral for OTC instruments; we pledged securities of \$544 million as collateral to counterparties.

We performed a sensitivity analysis on OTC derivative collateral requirements by assuming a hypothetical reduction in our S&P's insurance financial strength ratings from AA- to A and a 100 basis point decline in interest rates. The analysis indicated that we would have to post an estimated \$449 million in additional collateral. The selection of these hypothetical scenarios should not be construed as our prediction of future events, but only as an illustration of the estimated potential effect of such events. We also actively manage our counterparty credit risk exposure by monitoring the level of collateral posted by our counterparties with respect to our receivable positions.

To calculate the duration gap between assets and liabilities, we project asset and liability cash flows and calculate their net present value using a risk-free market interest rate adjusted for credit quality, sector attributes, liquidity and other specific risks. Duration is calculated by revaluing these cash flows at alternative interest rates and determining the percentage change in aggregate fair value. The cash flows used in this calculation include the

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expected maturity and repricing characteristics of our derivative financial instruments, all other financial instruments (as described in Note 7 of the consolidated financial statements), and certain other items including annuity liabilities and other interest-sensitive liabilities. The projections include assumptions (based upon historical market experience and our experience) that reflect the effect of changing interest rates on the prepayment, lapse, leverage and/or option features of instruments, where applicable. The preceding assumptions relate primarily to mortgage-backed securities, collateralized mortgage obligations, municipal housing bonds, callable municipal and corporate obligations, and fixed rate single and flexible premium deferred annuities.

Based upon the information and assumptions used in the duration calculation, and interest rates in effect at December 31, 2008, we estimate that a 100 basis point immediate, parallel increase in interest rates ("rate shock") would decrease the net fair value of the assets and liabilities by approximately \$169 million, compared to \$449 million at December 31, 2007. In calculating the impact of a 100 basis point increase on the value of the derivatives, we have assumed interest rate volatility remains constant. The selection of a 100 basis point immediate parallel change in interest rates should not be construed as our prediction of future market events, but only as an illustration of the potential effect of such an event. There are \$6.19 billion of assets supporting life insurance products such as traditional and interest-sensitive life that are not financial instruments. These assets and the associated liabilities have not been included in the above estimate. The \$6.19 billion of assets excluded from the calculation has decreased from the \$7.05 billion reported at December 31, 2007 due to capital market changes. Based on assumptions described above, in the event of a 100 basis point immediate increase in interest rates, the assets supporting life insurance products would decrease in value by \$487 million, compared to a decrease of \$521 million at December 31, 2007.

To the extent that conditions differ from the assumptions we used in these calculations, duration and rate shock measures could be significantly impacted. Additionally, our calculations assume that the current relationship between short-term and long-term interest rates (the term structure of interest rates) will remain constant over time. As a result, these calculations may not fully capture the effect of non-parallel changes in the term structure of interest rates and/or large changes in interest rates.

CREDIT SPREAD RISK is the risk that we will incur a loss due to adverse changes in credit spreads ("spreads"). This risk arises from many of our primary activities, as we invest substantial funds in spread-sensitive fixed income assets.

We manage the spread risk in our assets. One of the measures used to quantify this exposure is spread duration. Spread duration measures the price sensitivity of the assets to changes in spreads. For example, if spreads increase 100 basis points, the fair value of an asset exhibiting a spread duration of 5 is expected to decrease in value by approximately 5%.

Spread duration is calculated similarly to interest rate duration. At December 31, 2008, the spread duration of assets was 4.3. Based upon the information and assumptions we use in this spread duration calculation, and spreads in effect at December 31, 2008, we estimate that a 100 basis point immediate, parallel increase in spreads across all asset classes, industry sectors and credit ratings ("spread shock") would decrease the net fair value of the assets by approximately \$2.19 billion, compared to \$3.12 billion at December 31, 2007. Reflected in the duration calculation are the effects of our risk mitigation actions that use credit default swaps to manage spread risk. Based on contracts in place at December 31, 2008, we would recognize realized capital gains totaling \$35 million in the event of a 100 basis point immediate, parallel spread increase and \$35 million in realized capital losses in the event of a 100 basis point immediate, parallel spread decrease. The selection of a 100 basis point immediate parallel change in spreads should not be construed as our prediction of future market events, but only as an illustration of the potential effect of such an event.

EQUITY PRICE RISK is the risk that we will incur losses due to adverse changes in the general levels of the equity markets. At December 31, 2008, we held approximately \$1.86 billion in securities with equity risk (including primarily convertible securities, limited partnership interests, non-redeemable preferred securities and equity-linked notes), compared to \$1.82 billion at December 31, 2007. Additionally, we had 508 contracts in short equity index futures at December 31, 2008 with a fair value of \$23 million.

At December 31, 2008, our portfolio of securities with equity risk had a cash market portfolio beta of approximately 0.45, compared to a beta of approximately 0.89 at December 31, 2007. Beta represents a widely used methodology to describe, quantitatively, an investment's market risk characteristics relative to an index such as the S&P 500. Based on the beta analysis, we estimate that if the S&P 500 increases or decreases by 10%, the fair value of our equity investments will increase or decrease by approximately 4.5%, respectively. Based upon the information and assumptions we used to calculate beta at December 31, 2008, including the effect of the equity index futures, we estimate that an immediate decrease in the S&P 500 of 10% would decrease the net fair value of our equity investments identified above by approximately \$82 million, compared to \$164 million at December 31, 2007, and an immediate increase in the S&P 500 of 10% would increase the net fair value by \$82 million compared to \$164 million at December 31,

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2007. In calculating the impact of a 10% S&P index perturbation on the value of the futures, we have assumed index volatility remains constant. Based on the equity index futures in place at December 31, 2008, we would recognize losses totaling \$2 million in the event of a 10% increase in the S&P 500 index and \$2 million in gains in the event of a 10% decrease. The selection of a 10% immediate decrease in the S&P 500 should not be construed as our prediction of future market events, but only as an illustration of the potential effect of such an event.

The beta of our securities with equity risk was determined using Barra's predictive beta. This beta is based on a company's fundamental data. The illustrations noted above may not reflect our actual experience if the future composition of the portfolio (hence its beta) and correlation relationships differ from the historical relationships.

At December 31, 2008 and 2007, we had separate accounts assets related to variable annuity and variable life contracts with account values totaling \$8.24 billion and \$14.93 billion, respectively. Equity risk exists for contract charges based on separate account balances and guarantees for death and/or income benefits provided by our variable products. In 2006, we disposed of substantially all of the variable annuity business through a reinsurance agreement with Prudential as described in Note 3 of the consolidated financial statements, and therefore mitigated this aspect of our risk. Equity risk of our variable life business relates to contract charges and policyholder benefits. Total variable life contract charges for 2008 and 2007 were \$95 million and \$92 million, respectively. Separate account liabilities related to variable life contracts were \$561 million and \$905 million in December 31, 2008 and 2007,

respectively.

At December 31, 2008 and 2007 we had approximately \$4.11 billion and \$3.98 billion, respectively, in equity-indexed annuity liabilities that provide customers with interest crediting rates based on the performance of the S&P 500. We hedge the risk associated with these liabilities using equity-indexed options and futures, interest rate swaps, and eurodollar futures, maintaining risk within specified value-at-risk limits.

FOREIGN CURRENCY EXCHANGE RATE RISK is the risk that we will incur economic losses due to adverse changes in foreign currency exchange rates. This risk primarily arises from the foreign component of our limited partnership interests. We also have certain funding agreement programs and a small amount of fixed income securities that are denominated in foreign currencies, however, derivatives are used to hedge the foreign currency risk of these funding agreements and fixed income securities. At December 31, 2008 and 2007, we had approximately \$713 million and \$924 million, respectively, in funding agreements denominated in foreign currencies.

At December 31, 2008, the foreign component of our limited partnership interests totaled approximately \$228 million, compared to \$158 million at December 31, 2007. Based upon the information and assumptions used at December 31, 2008, we estimate that a 10% immediate unfavorable change in each of the foreign currency exchange rates that we are exposed to would decrease the value of the foreign component of our limited partnership interests by approximately \$23 million, compared with an estimated \$16 million decrease at December 31, 2007. The selection of a 10% immediate decrease in all currency exchange rates should not be construed as our prediction of future market events, but only as an illustration of the potential effect of such an event. Our currency exposure is diversified across 33 currencies, compared to 27 currencies at December 31, 2007. Our largest individual foreign currency exposures at December 31, 2008 were to the Euro (35.5%) and the British Pound (16.1%). The largest individual foreign currency exposures at December 31, 2007 were to the Euro (41.1%) and the British Pound (21.7%). Our primary regional exposure is to Western Europe, approximately 61.1% at December 31, 2008, compared to 65.0% at December 31, 2007.

The modeling technique we use to report our currency exposure does not take into account correlation among foreign currency exchange rates. Even though we believe it is very unlikely that all of the foreign currency exchange rates that we are exposed to would simultaneously decrease by 10%, we nonetheless stress test our portfolio under this and other hypothetical extreme adverse market scenarios. Our actual experience may differ from these results because of assumptions we have used or because significant liquidity and market events could occur that we did not foresee.

DEFERRED TAXES

The total deferred tax valuation allowance is \$9 million at December 31, 2008. We evaluate whether a valuation allowance is required each reporting period. A valuation allowance is established if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred income tax asset will not be realized. In determining whether a valuation allowance is needed, all available evidence is considered. This includes the potential for capital and ordinary loss carryback, future reversals of existing taxable temporary differences, tax planning strategies and future taxable income exclusive of reversing temporary differences.

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With respect to our evaluation of the need for a valuation allowance related to the deferred tax asset on unrealized losses on fixed income securities, we rely on our assertion that we have the intent and ability to hold the securities to recovery. As a result, the unrealized losses on these securities would not be expected to materialize and no valuation allowance on the associated deferred tax asset is needed.

With respect to our evaluation of the need for a valuation allowance related to other capital losses that have not yet been recognized for tax purposes, we utilize prudent and feasible tax planning strategies. These include strategies that optimize The Allstate Corporation's (the "Corporation's") ability to carry back capital losses as well as the ability to offset future capital losses with capital gains that could be recognized for tax purposes. Changes in the market value of our investments may impact the level of capital gains and losses that can be used in the tax planning strategies. The \$9 million valuation allowance at December 31, 2008 relates to the deferred tax asset on capital losses that have not yet been recognized for tax purposes.

CAPITAL RESOURCES AND LIQUIDITY

("Superior")
Standard &
Poor's
Ratings
Services
AA- ("Very
Strong")
Moody's
Investors
Service,
Inc. A1
("Good")

Our ratings are influenced by many factors including our operating and financial performance, asset quality, liquidity, asset/liability management, overall portfolio mix, financial leverage (i.e., debt), exposure to risks, operating leverage, AIC's ratings and other factors.

On February 2, 2009, A.M. Best affirmed our A+ financial strength rating. On January 29, 2009, S&P downgraded our financial strength rating to AA- from AA. The outlook for the rating remained negative. In October 2008, the outlook had been revised to negative from stable. On January 29, 2009, Moody's downgraded our financial strength rating to A1 from Aa3. The outlook for the rating was revised to stable from negative. In October 2008, Moody's downgraded our financial strength rating to Aa3 from Aa2.

Effective May 8, 2008, the Company, AIC and the Corporation entered into a one-year Amended and Restated Intercompany Liquidity Agreement ("Liquidity Agreement") replacing the Intercompany Liquidity Agreement between the Company and AIC dated January 1, 2008. The Liquidity Agreement allows for short-term advances of funds to be made between parties for liquidity and other general corporate purposes. It shall be automatically renewed for subsequent one-year terms unless terminated by the parties. The Liquidity Agreement does not establish a commitment to advance funds on the part of either party. The Company and AIC each serve as a lender and borrower and the Corporation serves only as a lender. The Company also has a capital support agreement with

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AIC effective December 14, 2007. Under the capital support agreement, AIC is committed to provide capital to the Company to allow for profitable growth while maintaining an adequate capital level. The maximum amount of potential funding under the intercompany liquidity and capital support agreements is \$1.00 billion. See Note 5 to the consolidated financial statements for further details.

Our life insurance subsidiaries prepare their statutory-basis financial statements in conformity with accounting practices prescribed or permitted by the insurance department of the applicable state of domicile. Statutory surplus is a measure that is often used as a basis for determining dividend paying capacity, operating leverage and premium growth capacity, and it is also reviewed by rating agencies in determining their ratings. As of December 31, 2008, ALIC's statutory surplus is \$3.25 billion at December 31, 2008, compared to \$2.62 billion at December 31, 2007.

We have received approval from the Illinois Division of Insurance for the use of two permitted practices in the statutory-basis financial statements related to areas in which statutory accounting is not reflective of the underlying economics during this period of extreme market conditions caused by the current economic crisis. The first permitted practice relates to the statutory accounting for deferred taxes and applies to ALIC. Specifically, this permitted practice increased the amount of deferred income tax asset that can be recognized in the statutory-basis financial statements and included in statutory surplus from the lesser of the amounts that can be realized in one year or 10% of adjusted statutory surplus to the lesser of deferred taxes that can be realized within 3 years or 15% of adjusted statutory surplus. The permitted practice resulted in an increase in ALIC's statutory surplus of \$140 million as of December 31, 2008. Admitted statutory-basis deferred tax assets totaled \$421 million after the permitted practice reflecting 52% of total potential statutory-basis deferred tax assets before non-admission limitations. The second permitted practice relates to statutory accounting for market value adjusted annuities ("MVAA") whose related assets are held in a separate account in the statutory-basis financial statements and applies to ALIC. Specifically, this permitted practice resulted in the MVAA related investments being recorded at amortized cost, which is consistent with statutory accounting for other fixed income investments and the book value method of accounting required under Illinois Code for MVAA investments held in a general account. The permitted practice was requested because the Illinois Code is silent on MVAA that are issued by a separate account. In the extreme market conditions of the economic

crisis, the market value method of accounting reduced statutory surplus due to unrealized losses on investments caused by wide credit spreads and the liquidity based dislocations in the investment markets in a manner not representative of the economics of the related liabilities. The effect of the permitted practice, which is to value the invested assets and insurance reserves on a book value basis instead of the formerly used market value basis, was \$394 million based on October 1, 2008 valuations and grew to \$1.24 billion at December 31, 2008 due to an increase of \$720 million in the investment unrealized loss position, while the market-based reserves increased \$130 million relative to book-basis reserves. The permitted practice eliminated the inconsistent impacts in the amounts determined by the valuation methodologies for invested assets and insurance reserves and resulted in invested assets being valued at \$8.07 billion and reserves at \$9.17 billion.

State laws specify regulatory actions if an insurer's risk-based capital ("RBC"), a measure of an insurer's solvency, falls below certain levels. The NAIC has a standard formula for annually assessing RBC. The formula for calculating RBC for life insurance companies takes into account factors relating to insurance, business, asset and interest rate risks. At December 31, 2008, the RBC for each of our insurance companies was within the range that we target.

The NAIC has also developed a set of financial relationships or tests known as the Insurance Regulatory Information System to assist state regulators in monitoring the financial condition of insurance companies and identifying companies that require special attention or actions by insurance regulatory authorities. The NAIC analyzes financial data provided by insurance companies using prescribed ratios, each with defined "usual ranges". Generally, regulators will begin to monitor an insurance company if its ratios fall outside the usual ranges for four or more of the ratios. If an insurance company has insufficient capital, regulators may act to reduce the amount of insurance it can issue. The ratios of our insurance companies are within these ranges.

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LIQUIDITY SOURCES AND USES Our potential sources of funds principally include the activities as follows.

- Receipt of insurance premiums
- Contractholder fund deposits
- Reinsurance recoveries
- Receipts of principal, interest and dividends on investments
- Sales of investments
- Funds from investment repurchase agreements, securities lending, and line of credit agreements
- Intercompany loans
- Capital contributions from parent
- Tax refunds/settlements

Our potential uses of funds principally include the activities as follows.

- Payment of contract benefits, maturities, surrenders and withdrawals
- Reinsurance cessions and payments
- Operating costs and expenses
- Purchase of investments
- Repayment of investment repurchase agreements, securities lending, and line of credit agreements
- Payment or repayment of intercompany loans
- Dividends to parent
- Debt service expenses and repayment

We actively manage our financial position and liquidity levels in light of changing market, economic, and business conditions. In 2008, in anticipation of continued volatility and illiquidity in the financial markets, we took actions to enhance our economic and liquidity position pending a return to normal capital market conditions. These actions included:

- Managing our gross exposure to our largest tail risk exposure, interest rate risk, through active management of our investment and product portfolios as well as further mitigation through hedging.
- Accumulating higher cash and short-term investment positions easily convertible to cash from asset sales, principal and interest receipts, calls, maturities and other cash inflows from our investment portfolio.
- Reducing our securities lending program to \$364 million as of December 31, 2008 from \$1.78 billion as of December 31, 2007. By reducing the securities lending program, we gained additional direct access to our liquid investments.
- Proactively selling securities we think will become less liquid.

We believe that these actions will provide us with a greater level of flexibility necessary to operate in the current market environment. If market conditions warrant, we may take additional actions to enhance our liquidity position including:

- Continued retention of portfolio cash flows including approximately \$7.20 billion of expected inflows from upcoming maturities, calls and prepayments on fixed income securities, mortgage loans and bank loans, and interest receipts on investments over the next twelve months. Expected interest receipts include amounts related to floating rate investments for which the interest rate fluctuates in accordance with market interest rates. Our expectation is based on market interest rates as of December 31, 2008. Further, these expected portfolio cash flows are based on investments as of December 31, 2008 and were determined without regard to increases in the portfolio for reasons such as the reinvestment of portfolio cash flows or decreases due to reductions in outstanding contractholder funds obligations.
- The sale of fixed income securities (government, municipal and investment grade corporate bonds) with unrealized capital gains at December 31, 2008.

With a focus on preserving capital, we consider investments which are convertible to cash without generating significant additional net realized capital losses as liquidity sources. The following table presents cash and short-term positions easily convertible to cash, and certain other liquid investments meeting these criteria.

AS OF (\$ IN MILLIONS) DECEMBER 31, 2008 -- ----- ----- Cash and short- term positions easily convertible to cash available same day/next day \$ 2,648 Other highly liquid investments (1) 1,271 Other liquid investments (2) 2,219 - ----- Total liquid \$ 6,138 =====
Percent of total consolidated cash and investments 10.3%

- (1) Other highly liquid investments are defined as assets that are generally saleable within one week, and primarily include U.S. government and agencies bonds of \$598 million, short-term investments of \$234 million, corporate bonds of \$206 million, agency pass through securities of \$109 million and foreign sovereign securities of \$100 million. The amounts shown in the table above represent the amount of our holdings in these assets, excluding any holdings with restrictions.
- (2) Other liquid investments are defined as assets that

are saleable within one quarter, and primarily include short-term investments of \$703 million, corporate bonds of \$679 million, U.S. government and agencies bonds of \$350 million and agency pass through securities of \$109 million. The amounts shown in the table above represent the amount that we believe could be sold during the first quarter of 2009, excluding any holdings with restrictions.

The above analysis identifies our access to internal sources of liquidity. We believe we have sufficient liquidity to address current planned needs from investments other than those for which we have asserted the intent to hold until recovery combined with targeted sales of certain products. Additionally, we have existing intercompany agreements in place that facilitate liquidity management.

To increase new money for investing, we have initiated actions to accelerate the recovery of approximately \$500 million of tax refunds from the overpayment of 2008 estimated taxes as well as the carryback of 2008 ordinary losses to prior tax years. \$60 million in refunds were received in March 2009 and we expect the remaining refunds to be received in the first half of 2009.

ALLSTATE PARENT COMPANY CAPITAL CAPACITY The Allstate Corporation has at the parent holding company level, deployable cash and investments totaling \$3.64 billion as of December 31, 2008. These assets include highly liquid securities that are generally saleable within one week totaling \$2.29 billion, additional liquid investments that are saleable within one quarter totaling \$972 million, and \$381 million of investments that trade in illiquid markets. The substantial earnings capacity of the operating subsidiaries is the primary source of capital generation for the Corporation. In 2009, AIC will have the capacity to pay dividends currently estimated at \$1.30 billion without prior regulatory approval. We do not anticipate that the Company will pay dividends to AIC in 2009. In addition, the Corporation has access to \$1.00 billion of funds from either commercial paper issuance or an unsecured revolving credit facility. This provides capital for the parent company's relatively low fixed charges, estimated at \$650 million in 2009, and \$750 million of debt maturing in December 2009, to the extent not refinanced prior to maturity.

In October 2008, the Corporation completed its previously approved capital contribution of \$1.00 billion of invested assets to AIC. In November 2008, AIC purchased a \$400 million surplus note from the Company and made a capital contribution of \$600 million to the Company. An additional amount of approximately \$250 million remains under the authority granted by the Corporation and AIC boards on October 15, 2008 and October 20, 2008, respectively, to make capital contributions in the form of cash and securities, by providing a guaranty or guaranties, or by purchasing one or more surplus notes or other securities on or before April 30, 2009.

Moreover, in addition to these historic external sources of capital, access to funding from additional sources, including participation in programs offered by the U.S. Treasury and other governmental organizations, are potentially available to the Corporation and its operating subsidiaries for capital and liquidity needs.

The Company has access to additional borrowing to support liquidity through the Corporation as follows:

- - A commercial paper facility with a borrowing limit of \$1.00 billion to cover short-term cash needs. As of December 31, 2008, there were no balances outstanding and therefore the remaining borrowing capacity was \$1.00 billion; however, the outstanding balance fluctuates daily.
- - A primary credit facility is available for short-term liquidity requirements and backs a commercial paper facility. The \$1.00 billion unsecured revolving credit facility, has an initial term of five years expiring in 2012 with two

optional one-year extensions that can be exercised at the end of any of the remaining four years of the facility upon approval of existing or replacement lenders providing more than two-thirds of the commitments to lend. The program is fully subscribed among 11 lenders with the largest commitments being \$185 million. The commitments of the lenders are several and no lender is responsible for any other lender's commitment if such lender fails to make a loan under the facility. None of the borrowing capacity under this credit facility has been utilized. This facility contains an increase provision that would allow up to an additional \$500 million of borrowing provided the increased portion could be fully syndicated at a later date among existing or new lenders. This facility has a financial covenant requiring that the Corporation not exceed a 37.5% debt

to capital resources ratio as defined in the agreement. This ratio at December 31, 2008 was 20.5%. Although the right to borrow under the facility is not subject to a minimum rating requirement, the costs of maintaining the facility and borrowing under it are based on the ratings of the Corporation's senior, unsecured, nonguaranteed long-term debt. There were no borrowings under this line of credit during 2008. The total amount outstanding at any point in time under the combination of the commercial paper program and the credit facility cannot exceed the amount that can be borrowed under the credit facility.

- - A universal shelf registration statement was filed by the Corporation with the Securities and Exchange Commission ("SEC") in May 2006 and will expire May 2009. In April 2009, the Corporation expects to ask its board of directors for authority to file a replacement universal shelf registration. The Corporation can use the current shelf registration to issue an unspecified amount of debt securities, common stock (including 364 million shares of treasury stock as of December 31, 2008), preferred stock, depository shares, warrants, stock purchase contracts, stock purchase units and securities of subsidiaries. The specific terms of any securities the Corporation issues under this registration statement will be provided in the applicable prospectus supplements.

LIQUIDITY EXPOSURE Contractholder funds as of December 31, 2008 were \$56.78 billion. The following table summarizes contractholder funds by their contractual withdrawal provisions at December 31, 2008.

% TO (\$ IN MILLIONS)	TOTAL -----
--- Not subject to discretionary withdrawal \$	13,337 23.5%
Subject to discretionary withdrawal with adjustments: Specified surrender charges (1)	25,440 44.8
Market value adjustments (2) 9,586	16.9
Subject to discretionary withdrawal without adjustments (3) 8,417	14.8 -----
----- - Total contractholder funds (4) \$	56,780 100.0%
=====	
=====	

- (1) Includes approximately \$10.99 billion of liabilities with a contractual surrender charge of less than 5% of the account balance.
- (2) Approximately \$7.96 billion of the contracts with market value adjusted surrenders have a 30-45 day period during which there is no surrender charge or market value adjustment.
- (3) Includes extendible funding agreements backing medium-term notes outstanding with a par value of \$1.45 billion that have been non-extended, of which \$1.21 billion has been called and will be retired in March 2009 and the remainder will become due by July 31, 2009. We have accumulated, and expect to maintain, short-term and other maturing investments to fund the retirement of these obligations.
- (4) Includes approximately \$1.47 billion of contractholder funds on variable annuities reinsured to Prudential effective June 1, 2006.

While we are able to quantify scheduled maturities for our institutional products of \$3.25 billion in 2009, anticipating retail product surrenders is less precise. Retail life and annuity products may be surrendered by customers for a variety of reasons. Reasons unique to individual customers include a current or unexpected need for cash or a change in life insurance coverage needs. Other key factors that may impact the likelihood of customer surrender include the level of the contract surrender charge, the length of time the contract has been in force, distribution channel, market interest rates, equity market conditions and potential tax implications. In addition, the propensity for retail life insurance policies to lapse is lower than it is for fixed annuities because of the need for the insured to be re-underwritten upon policy replacement. Surrenders and partial withdrawals for our retail annuities decreased 13.9% in 2008 compared to 2007. The annualized surrender and partial withdrawal rate on deferred annuities and interest-sensitive life insurance products, based on the beginning of year contractholder funds, was 10.3% and 11.6% in 2008 and 2007, respectively. The Company strives to promptly pay customers who request cash surrenders, however, statutory regulations generally provide up to six months in most states to fulfill surrender requests.

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Our institutional products are primarily funding agreements backing medium-term notes. As of December 31, 2008, total institutional products outstanding were \$8.94 billion. The following table presents the scheduled maturities for our institutional products outstanding as of December 31, 2008.

(\$ IN
MILLIONS)
2009 \$ 3,249
2010 3,059
2011 760
2012 40
2013 1,750
2016 85

---- \$ 8,943
=====

Our asset-liability management practices limit the differences between the cash flows generated by our investment portfolio and the expected cash flow requirements of our life insurance, annuity and institutional product obligations.

Certain events and circumstances could constrain our, the Corporation's or AIC's liquidity. Those events and circumstances include, for example, a catastrophe resulting in extraordinary losses, a downgrade in the Corporation's long-term debt rating of A3, A- and a- (from Moody's, S&P's and A.M. Best, respectively) to non-investment grade status of below Baa3/BBB-/bb, a downgrade in AIC's financial strength rating from Aa3, AA- and A+ (from Moody's, S&P's and A.M. Best, respectively) to below Baa2/BBB/A-, or a downgrade in our financial strength ratings from A1, AA- and A+ (from Moody's, S&P's and A.M. Best, respectively) to below A1/AA-/A-. The rating agencies also consider the interdependence of our individually rated entities, therefore, a rating change in one entity could potentially affect the ratings of other related entities.

CASH FLOWS As reflected in our Consolidated Statements of Cash Flows, lower operating cash flows in 2008, compared to 2007, were primarily related to a decrease in investment income, partially offset by higher premiums and income tax refunds in 2008 compared to income taxes paid in 2007. Higher operating cash flows in 2007, compared to 2006, primarily related to lower operating expenses and tax payments, and an increase in investment income, partially offset by increased policy and contract benefit payments and the absence in 2007 of contract charges on the reinsured variable annuity business.

Cash flows provided by investing activities increased in 2008 compared to 2007, primarily due to decreased purchases of fixed income securities and mortgage loans, partially offset by lower investment collections and net change in short-term investments. Cash flows from investing activities increased in 2007, compared to 2006, primarily due to increased cash provided by operating activities, partially offset by increased cash used in financing activities.

Higher cash flows used in financing activities in 2008 compared to 2007 were primarily due to higher maturities and retirements of institutional products, partially offset by higher contractholder fund deposits. Cash flows used in financing activities increased in 2007, compared to 2006, primarily due to lower contractholder fund deposits. For further quantification of the changes in contractholder funds, see the Operations section of MD&A.

There were no dividends paid by the Company in 2008. In 2007 and 2006,

27,610 \$
12,836 \$
56,336

=====
=====
=====
=====
=====

-
- (1) Liabilities for collateral and repurchase agreements are typically fully secured with cash. We manage our short-term liquidity position to ensure the availability of a sufficient amount of liquid assets to extinguish short-term liabilities as they come due in the normal course of business, including utilizing potential sources of liquidity as disclosed previously.
 - (2) Contractholder funds represent interest-bearing liabilities arising from the sale of products such as interest-sensitive life, fixed annuities, including immediate annuities without life contingencies, and institutional products. The reserve for life-contingent contract benefits relates primarily to traditional life and immediate annuities with life contingencies. These amounts reflect the present value of estimated cash payments to be made to contractholders and policyholders. We are able to quantify scheduled payments related to our immediate annuities without life contingencies and institutional products with reasonable certainty, however, estimates of anticipated payments related to interest-sensitive life, fixed deferred annuities, traditional life and immediate annuities with life contingencies are subject to contractholder discretion and are therefore more variable. Immediate annuities without life contingencies and institutional products, involve payment obligations where the amount and timing of the payment is essentially fixed and determinable. These amounts relate to (i) policies or contracts where we are currently making payments and will continue to do so and (ii) contracts where the timing of a portion or all of the payments has been determined by the contract. Extendible funding agreements backing medium-term notes outstanding are reflected in the table above at the maturity date accelerated in accordance with the contractholders' election to not extend the maturity date. Other contracts, such as interest-sensitive life, fixed deferred annuities, traditional life and immediate annuities with life contingencies, involve payment obligations where a portion or all of the amount and timing of future payments is uncertain. For these contracts, the Company is not currently making payments and will not make payments until (i) the occurrence of an insurable event, such as death or illness or (ii) the occurrence of a payment triggering event such as the surrender of or partial withdrawal on a policy or deposit contract, which is outside of the control of the Company. We have estimated the timing of payments related to these contracts based on historical experience and our expectation of future payment patterns. Uncertainties relating to these liabilities include mortality, morbidity, expenses, customer lapse and withdrawal activity, estimated additional deposits for interest-sensitive life contracts, and renewal premium for life policies, which may significantly impact both the timing and amount of future payments. Such cash outflows reflect adjustments for the estimated timing of mortality, retirement, and other appropriate factors, but are undiscounted with respect to interest. As a result, the sum of the cash outflows shown for all years in the table exceeds the corresponding liabilities of \$56.78 billion for contractholder funds and \$12.26 billion for reserve for life-contingent contract benefits as included in the Consolidated Statements of Financial Position as of December 31, 2008. The liability amount in the Consolidated Statements of Financial Position reflects the discounting for interest as well as adjustments for the timing of other factors as described above.
 - (3) Amounts estimated to be paid out of contractholder funds in 1-3 years totaling \$23.96 billion includes amounts expected to be paid in 2010 of \$8.90 billion, 2011 of \$8.48 billion and 2012 of \$6.58 billion.
 - (4) Amounts estimated to be paid out of reserve for life-contingent contract benefits in 1-3 years totaling \$3.55 billion includes amounts expected to be paid in 2010 of \$1.20 billion, 2011 of \$1.17 billion and 2012 of \$1.18 billion.
 - (5) Amount differs from the balance presented on the Consolidated Statements of Financial Position as of December 31, 2008 because the surplus notes due to related parties as presented in the table above includes interest.
 - (6) Other liabilities primarily include accrued expenses, claim payments and other checks outstanding.
 - (7) Balance sheet liabilities not included in the table above include unearned and advanced premiums of \$40 million and deferred tax liabilities of \$801 million netted in the net deferred tax asset of \$1.38 billion. These items were excluded as they do not meet the definition of a contractual liability as we are not contractually obligated to pay these amounts to third parties. Rather, they represent an accounting mechanism that allows us to present our financial statements on an accrual basis. In addition, other

liabilities of \$746 million were not included in the table above because they did not represent a contractual obligation or the amount and timing of their eventual payment was sufficiently uncertain.

The following is a distribution in U.S. Dollars of funding agreements (non-putable) by currency at December 31. All foreign currency denominated funding agreements have been swapped to U.S. Dollars.

(\$ IN
MILLIONS)
2008 2007

CURRENCY
United
States
Dollar \$
8,230 \$
12,000
British
Pound 435
646 Swiss
Franc 278
278 -----

----- \$
8,943 \$
12,924
=====

Our contractual commitments as of December 31, 2008 and the periods in which the commitments expire are shown in the following table.

LESS THAN
OVER 5 (\$ IN
MILLIONS)
TOTAL 1 YEAR
1-3 YEARS 4-
5 YEARS
YEARS -----

Other
commitments
-
conditional
\$ 3 \$ 3 \$ --
\$ -- \$ --
Other
commitments
-
unconditional
(1) 1,077 95
573 379 30 -

----- Total
commitments
\$ 1,080 \$ 98
\$ 573 \$ 379
\$ 30
=====

(1) Unconditional other contractual commitments scheduled to expire in 1-3 years totaling \$573 million includes amounts scheduled to expire in 2010 of \$136 million, 2011 of \$200 million and 2012 of \$237 million.

Contractual commitments in the table above represent commitments to invest in limited partnership interests and commitments to extend mortgage loans. The funding of these commitments is largely contingent upon circumstances or events outside of our control, including those at the discretion of our counterparties. As a result, the timing of the funding of these commitments cannot be estimated and may occur at anytime prior to the expiration.

We have agreements in place for services we conduct, generally at cost, between subsidiaries relating to insurance, reinsurance, loans and capitalization. All material intercompany transactions have appropriately been eliminated in consolidation. Intercompany transactions among insurance subsidiaries and affiliates have been approved by the appropriate departments of insurance as required.

For a more detailed discussion of our off-balance sheet arrangements, see Note 7 of the consolidated financial statements.

REGULATION AND LEGAL PROCEEDINGS

We are subject to extensive regulation and we are involved in various legal and regulatory actions, all of which have an effect on specific aspects of our business. For a detailed discussion of the legal and regulatory actions in which we are involved, see Note 11 of the consolidated financial statements.

PENDING ACCOUNTING STANDARDS

There are several pending accounting standards that we have not implemented either because the standard has not been finalized or the implementation date has not yet occurred. For a discussion of these pending standards, see Note 2 of the consolidated financial statements.

The effect of implementing certain accounting standards on our financial results and financial condition is often based in part on market conditions at the time of implementation of the standard and other factors we are unable to determine prior to implementation. For this reason, we are sometimes unable to estimate the effect of certain pending accounting standards until the relevant authoritative body finalizes these standards or until we implement them.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Information required for Item 7A is incorporated by reference to the material under the caption "Market Risk" in Part II, Item 7 of this report.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

YEAR ENDED
DECEMBER 31,

- (\$ IN
MILLIONS)
2008 2007
2006 -----
-- -----

REVENUES
Premiums (net
of
reinsurance
ceded of
\$534, \$625
and \$617) \$
585 \$ 502 \$
576 Contract
charges (net
of
reinsurance
ceded of
\$340, \$315
and \$170) 911
942 1,009 Net
investment
income 3,720
4,205 4,057

Realized		
capital gains		
and losses		
(3,052)	(197)	
(79)	-----	
--	-----	

2,164	5,452	
5,563	COSTS	
AND EXPENSES		
Contract		
benefits (net		
of		
reinsurance		
recoveries of		
\$1,099, \$646		
and \$548)		
1,397	1,364	
1,372		
Interest		
credited to		
contractholder		
funds (net of		
reinsurance		
recoveries of		
\$43, \$47 and		
\$41)	2,356	
2,628	2,543	
Amortization		
of deferred		
policy		
acquisition		
costs	643	518
538	Operating	
costs and		
expenses	400	
340	398	-----

-	4,796	4,850
4,851	Loss on	
disposition		
of operations		
(4)	(10)	(88)

-----	(LOSS)	
INCOME FROM		
OPERATIONS		
BEFORE INCOME		
TAX EXPENSE		
(2,636)	592	
624	-----	

Income tax		
(benefit)		
expense	(946)	
180	196	-----

-	NET (LOSS)	
INCOME		
(1,690)	412	
428	-----	

OTHER		
COMPREHENSIVE		
LOSS, AFTER-		
TAX Change		
in:		
Unrealized		
net capital		
gains and		
losses		
(2,253)	(409)	
(263)	-----	

OTHER		

1,382 --
Other assets
1,294 622
Separate
Accounts
8,239 14,929

TOTAL ASSETS
\$ 81,946 \$
96,117

=====

=====

LIABILITIES

Contractholder
funds \$
56,780 \$
60,464

Reserve for
life-
contingent
contract
benefits
12,256 12,598

Unearned
premiums 32

33 Payable to
affiliates,
net 142 206

Other
liabilities
and accrued
expenses
1,638 2,823

Deferred
income taxes
-- 101

Surplus notes
due to
related
parties 650

200 Separate
Accounts
8,239 14,929

TOTAL
LIABILITIES
79,737 91,354

COMMITMENTS
AND
CONTINGENT
LIABILITIES
(NOTES 7 AND
11)

SHAREHOLDER'S
EQUITY

Redeemable
preferred
stock -
series A,
\$100 par
value,
1,500,000
shares
authorized,
none issued -
- - -

Redeemable
preferred
stock -
series B,
\$100 par
value,
1,500,000
shares
authorized,
none issued -
- - - Common

stock, \$227
 par value,
 23,800 shares
 authorized
 and
 outstanding 5
 5 Additional
 capital paid-
 in 2,475
 1,108
 Retained
 income 2,066
 3,734
 Accumulated
 other
 comprehensive
 loss:
 Unrealized
 net capital
 gains and
 losses
 (2,337) (84)

 Total
 accumulated
 other
 comprehensive
 loss (2,337)
 (84) -----

 TOTAL
 SHAREHOLDER'S
 EQUITY 2,209
 4,763 -----

 - TOTAL
 LIABILITIES
 AND
 SHAREHOLDER'S
 EQUITY \$
 81,946 \$
 96,117
 =====
 =====

See notes to consolidated financial statements.

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF SHAREHOLDER'S EQUITY

YEAR ENDED
 DECEMBER 31,

 ---- (\$ IN
 MILLIONS)
 2008 2007
 2006 -----

 - REDEEMABLE
 PREFERRED
 STOCK -
 SERIES A
 Balance,
 beginning of
 year \$ -- \$
 5 \$ 5
 Redemption
 of stock --
 (5) -- -----

 --- Balance,
 end of year

-- -- 5 ----

REDEEMABLE
PREFERRED
STOCK -
SERIES B --

-- COMMON
STOCK 5 5 5

ADDITIONAL
CAPITAL
PAID-IN
Balance,
beginning of
year 1,108
1,108 1,108
Capital
contributions
1,349 -- --
Gain on
reinsurance
transaction
with
affiliate
(see Note 5)
18 -- -- --

Balance, end
of year
2,475 1,108
1,108 -----

-- RETAINED
INCOME
Balance,
beginning of
year 3,734
4,055 4,302
Net (loss)
income
(1,690) 412
428 Gain on
purchase of
investments
from AIC
(see Note 5)
22 -- --
Dividends --
(725) (675)
Cumulative
effect of a
change in
accounting
principle --
(8) -- -----

Balance,
end of year
2,066 3,734
4,055 -----

ACCUMULATED
OTHER
COMPREHENSIVE
(LOSS)
INCOME
Balance,
beginning of

year (84)
 325 588
 Change in
 unrealized
 net capital
 gains and
 losses
 (2,253)
 (409) (263)

 Balance, end
 of year
 (2,337) (84)
 325 -----

TOTAL
 SHAREHOLDER'S
 EQUITY \$
 2,209 \$
 4,763 \$
 5,498
 =====
 =====
 =====

See notes to consolidated financial statements.

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF CASH FLOWS

YEAR ENDED
 DECEMBER 31,

 - (\$ IN
 MILLIONS)
 2008 2007
 2006 -----

CASH FLOWS
 FROM
 OPERATING
 ACTIVITIES
 Net (loss)
 income \$
 (1,690) \$ 412
 \$ 428
 Adjustments
 to reconcile
 net (loss)
 income to net
 cash provided
 by operating
 activities:
 Amortization
 and other
 non-cash
 items (423)
 (289) (280)
 Realized
 capital gains
 and losses
 3,052 197 79
 Loss on
 disposition
 of operations
 4 10 88
 Interest
 credited to
 contractholder
 funds 2,356
 2,628 2,543

Changes in:
 Policy
 benefit and
 other
 insurance
 reserves
 (446) (290)
 (199)
 Unearned
 premiums (2)
 (1) (1)
 Deferred
 policy
 acquisition
 costs 47 (29)
 (205)
 Reinsurance
 recoverables
 (167) (276)
 (218) Income
 taxes (828)
 112 (122)
 Other
 operating
 assets and
 liabilities -
 - 104 93 ----

 -- Net cash
 provided by
 operating
 activities
 1,903 2,578
 2,206 -----

CASH FLOWS
 FROM
 INVESTING
 ACTIVITIES
 Proceeds from
 sales: Fixed
 income
 securities
 11,083 11,222
 12,290 Equity
 securities
 131 73 23
 Limited
 partnership
 interests 100
 181 114
 Mortgage
 loans 248 --
 -- Other
 investments
 135 156 265
 Investment
 collections:
 Fixed income
 securities
 2,530 2,981
 2,727
 Mortgage
 loans 800
 1,506 1,618
 Other
 investments
 95 383 447
 Investment
 purchases:
 Fixed income
 securities
 (6,498)
 (12,096)
 (16,246)
 Equity
 securities
 (133) (101)
 (282) Limited

partnership
interests
(410) (673)
(22) Mortgage
loans (1,115)
(2,637)
(2,159) Other
investments
(120) (693)
(754) Change
in short-term
investments,
net (4,529)
31 362 Change
in other
investments,
net (359) 30
9 Disposition
of operations
(3) (5) (826)

----- Net
cash provided
by (used in)
investing
activities
1,955 358
(2,434) -----

- CASH FLOWS
FROM

FINANCING
ACTIVITIES

Issuance of
surplus notes
to related
parties 800 -

- - Capital
contributions
607 - -

Note payable
to parent - -
(500) 500

Redemption of
redeemable
preferred
stock - - (11)
(26)

Contractholder
fund deposits
9,253 7,948
9,546

Contractholder
fund
withdrawals
(14,610)
(9,736)
(8,998)

Dividends
paid - - (725)
(675) -----

Net cash
(used in)
provided by
financing
activities
(3,950)
(3,024) 347 -

----- NET
(DECREASE)
INCREASE IN
CASH (92)
(88) 119 CASH
AT BEGINNING
OF YEAR 185

273 154 -----

- CASH AT END
OF YEAR \$ 93
\$ 185 \$ 273
=====

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL

BASIS OF PRESENTATION

The accompanying consolidated financial statements include the accounts of Allstate Life Insurance Company ("ALIC") and its wholly owned subsidiaries (collectively referred to as the "Company"). ALIC is wholly owned by Allstate Insurance Company ("AIC"), which is wholly owned by Allstate Insurance Holdings, LLC, a wholly owned subsidiary of The Allstate Corporation (the "Corporation"). These consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP"). All significant intercompany accounts and transactions have been eliminated.

To conform to the current year presentation, certain amounts in the prior years' consolidated financial statements and notes have been reclassified.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

NATURE OF OPERATIONS

The Company sells life insurance, retirement and investment products to individual and institutional customers. The principal individual products are fixed annuities and interest-sensitive, traditional and variable life insurance. The principal institutional product is funding agreements backing medium-term notes issued to institutional and individual investors. The following table summarizes premiums and contract charges by product.

(\$ IN MILLIONS)	
2008	2007
2006	-----
-----	-----
- PREMIUMS	
Traditional life insurance	
(1) \$ 368	\$ 260
Immediate annuities with life contingencies	
132	204
Accident, health and other	85
41	38
-----	-----
TOTAL PREMIUMS	585
502	576
CONTRACT CHARGES	
Interest-sensitive life insurance	

(1) 855 862
797 Fixed
annuities 55
79 73
Variable
annuities 1
1 139 -----

-- TOTAL
CONTRACT
CHARGES 911
942 1,009 --

----- TOTAL
PREMIUMS AND
CONTRACT
CHARGES \$
1,496 \$
1,444 \$
1,585
=====

(1) Beginning in 2008, certain ceded reinsurance premiums previously included as a component of traditional life insurance premiums were reclassified prospectively to be reported as a component of interest-sensitive life insurance contract charges. In 2007 and 2006, these ceded reinsurance premiums were \$90 million and \$53 million, respectively.

The Company, through several subsidiaries, is authorized to sell life insurance, retirement and investment products in all 50 states, the District of Columbia, Puerto Rico, the U.S. Virgin Islands and Guam. For 2008, the top geographic locations for statutory premiums and annuity considerations were Delaware, California, Florida and New York. No other jurisdiction accounted for more than 5% of statutory premiums and annuity considerations. The Company distributes its products to individuals through multiple distribution channels, including Allstate exclusive agencies, which include exclusive financial specialists, independent agents (including master brokerage agencies and workplace enrolling agents), financial service firms, such as banks and broker-dealers, and specialized structured settlement brokers.

The Company has exposure to market risk as a result of its investment portfolio. Market risk is the risk that the Company will incur realized and unrealized net capital losses due to adverse changes in equity, interest, credit spreads or currency exchange rates and prices. The Company's primary market risk exposures are to changes in interest rates and equity prices. Interest rate risk is the risk that the Company will incur a loss due to adverse changes in interest rates relative to the interest rate characteristics of its interest bearing assets and liabilities. This risk arises from many of the Company's primary activities, as it invests substantial funds in interest-sensitive assets

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

and issues interest-sensitive liabilities. Interest rate risk includes risks related to changes in U.S. Treasury yields and other key risk-free reference yields, as well as changes in interest rates resulting from widening credit spreads and credit exposure. Equity price risk is the risk that the Company will incur losses due to adverse changes in the general levels of the equity markets or equity-like investments.

The Company monitors economic and regulatory developments that have the potential to impact its business. The ability of banks to affiliate with insurers may have a material adverse effect on all of the Company's product lines by substantially increasing the number, size and financial strength of potential competitors. The Company currently benefits from agreements with financial services entities that market and distribute its products; change in control of these non-affiliated entities could negatively impact the Company's sales. Furthermore, federal and state laws and regulations affect the taxation of insurance companies and life insurance and annuity products. Congress and various state legislatures have considered proposals that, if enacted, could impose a greater tax burden on the Company or could have an adverse impact on the tax treatment of some insurance products offered by the Company, including

favorable policyholder tax treatment currently applicable to life insurance and annuities. Legislation that reduced the federal income tax rates applicable to certain dividends and capital gains realized by individuals, or other proposals, if adopted, that reduce the taxation or permit the establishment of certain products or investments that may compete with life insurance or annuities, could have an adverse effect on the Company's financial position or ability to sell such products and could result in the surrender of some existing contracts and policies. In addition, changes in the federal estate tax laws could negatively affect the demand for the types of life insurance used in estate planning.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

INVESTMENTS

Fixed income securities include bonds, asset-backed securities, mortgage-backed securities, commercial mortgage-backed securities and redeemable preferred stocks. Fixed income securities may be sold prior to their contractual maturity, are designated as available for sale and are carried at fair value. The difference between amortized cost and fair value, net of deferred income taxes, certain deferred policy acquisition costs ("DAC"), certain deferred sales inducement costs ("DSI"), and certain reserves for life-contingent contract benefits, is reflected as a component of accumulated other comprehensive income. Cash received from calls, principal payments and make-whole payments is reflected as a component of proceeds from sales and cash received from maturities and pay-downs is reflected as a component of investment collections within the Consolidated Statements of Cash Flows. Reported in fixed income securities are hybrid securities which have characteristics of fixed income securities and equity securities. Many of these securities have attributes most similar to those of fixed income securities such as a stated interest rate, a mandatory redemption date or an interest rate step-up feature which is intended to incent the issuer to redeem the security at a specified call date. Hybrid securities are carried at fair value and amounted to \$1.36 billion and \$2.67 billion at December 31, 2008 and 2007, respectively.

Equity securities primarily include common and non-redeemable preferred stocks and real estate investment trust equity investments. Common and non-redeemable preferred stocks and real estate investment trust equity investments are classified as available for sale and are carried at fair value. The difference between cost and fair value, net of deferred income taxes, is reflected as a component of accumulated other comprehensive income.

Mortgage loans are carried at outstanding principal balances, net of unamortized premium or discount and valuation allowances. Valuation allowances are established for impaired loans when it is probable that contractual principal and interest will not be collected. Valuation allowances for impaired loans reduce the carrying value to the fair value of the collateral or the present value of the loan's expected future repayment cash flows discounted at the loan's original effective interest rate.

Investments in limited partnership interests, including certain interests in limited liability companies, private equity/debt funds, real estate funds and hedge funds where the Company's interest is so minor that it exercises virtually no influence over operating and financial policies are accounted for in accordance with the cost method of accounting; otherwise, investments in limited partnership interests are accounted for in accordance with the equity method of accounting.

Short-term investments, including money market funds, commercial paper and other short-term investments, are carried at fair value. Policy loans are carried at the respective unpaid principal balances. Other investments consist primarily of bank loans. Bank loans are comprised primarily of senior secured corporate loans which are carried at amortized cost.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In connection with the Company's securities lending business activities, funds received in connection with securities repurchase agreements, cash collateral received from counterparties related to derivative transactions and securities purchased under agreements to resell are invested and classified as short-term investments or fixed income securities available for sale as applicable. For the Company's securities lending business activities, securities sold under agreements to repurchase and collateral received from counterparties related to derivative transactions, the Company records an offsetting liability in other liabilities and accrued expenses or other investments for the Company's obligation to return the collateral or funds received.

Investment income consists primarily of interest and dividends, income from certain limited partnership interests and income from certain derivative

transactions. Interest is recognized on an accrual basis using the effective yield method and dividends are recorded at the ex-dividend date. Interest income for asset-backed securities, mortgage-backed securities and commercial mortgage-backed securities is determined considering estimated principal repayments obtained from widely accepted third party data sources and internal estimates. Interest income on beneficial interests in securitized financial assets not of high credit quality is determined using the prospective yield method, based upon projections of expected future cash flows. For all other asset-backed securities, mortgage-backed securities and commercial mortgage-backed securities, the effective yield is recalculated on the retrospective basis. Accrual of income is suspended for fixed income securities, mortgage loans and bank loans that are in default or when receipt of interest payments is in doubt. Income from investments in limited partnership interests accounted for on the cost basis is recognized upon receipt of amounts distributed by the partnerships as investment income. Subsequent to October 1, 2008, income from investments in limited partnership interests accounted for utilizing the equity method of accounting ("EMA LP") is reported in realized capital gains and losses.

Realized capital gains and losses include gains and losses on investment sales, write-downs in value due to other-than-temporary declines in fair value, periodic changes in the fair value and settlements of certain derivatives including hedge ineffectiveness, and income from certain limited partnership interests. Realized capital gains and losses on investment sales include calls and prepayments and are determined on a specific identification basis. Income from investments in limited partnership interests accounted for utilizing the equity method of accounting is recognized based on the financial results of the entity and the Company's proportionate investment interest, and is recognized on a delay due to the availability of the related financial statements. The recognition of income on hedge funds is primarily on a one month delay and the income recognition on private equity/debt funds and real estate funds are generally on a three month delay.

The Company recognizes other-than-temporary impairment losses on fixed income securities, equity securities and short-term investments when the decline in fair value is deemed other than temporary including when the Company cannot assert a positive intent to hold an impaired security until recovery (see Note 6). Fixed income securities subject to change in intent write-downs continue to earn investment income (other than discussed above), and any discount or premium is recognized using the effective yield method over the expected life of the security.

FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

The Company adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 157, "Fair Value Measurements" ("SFAS No. 157"), as of January 1, 2008 for its financial assets and financial liabilities that are measured at fair value. SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, and establishes a framework for measuring fair value. The adoption did not have a material effect on the Company's determination of fair value.

In determining fair value, the Company principally uses the market approach which generally utilizes market transaction data for the same or similar instruments. To a lesser extent, the Company uses the income approach which involves determining fair values from discounted cash flow methodologies. SFAS No. 157 establishes a hierarchy for inputs used in determining fair value that maximize the use of observable inputs and minimizes the use of unobservable inputs by requiring that observable inputs be used when available.

Observable inputs are those used by market participants in valuing financial instruments that are developed based on market data obtained from independent sources. In the absence of sufficient observable inputs, unobservable inputs reflect the Company's estimates of the assumptions market participants would use in valuing financial assets and financial liabilities and are developed based on the best information available in the circumstances. The Company uses prices and inputs that are current as of the measurement date, including during

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

periods of market disruption. In periods of market disruption, the ability to observe prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified from Level 1 to Level 2, or from Level 2 to Level 3.

Financial assets and financial liabilities recorded on the Consolidated

Statements of Financial Position at fair value as of December 31, 2008 are categorized in the fair value hierarchy based on the observability of inputs to the valuation techniques as follows:

LEVEL 1: Financial assets and financial liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Company can access.

LEVEL 2: Financial assets and financial liabilities whose values are based on the following:

- a) Quoted prices for similar assets or liabilities in active markets;
- b) Quoted prices for identical or similar assets or liabilities in non-active markets; or
- c) Valuation models whose inputs are observable, directly or indirectly, for substantially the full term of the asset or liability.

LEVEL 3: Financial assets and financial liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect the Company's estimates of the assumptions that market participants would use in valuing the financial assets and financial liabilities.

The availability of observable inputs varies by instrument. In situations where fair value is based on internally developed pricing models or inputs that are unobservable in the market, the determination of fair value requires more judgment. The degree of judgment exercised by the Company in determining fair value is typically greatest for instruments categorized in Level 3. In many instances, valuation inputs used to measure fair value fall into different levels of the fair value hierarchy. The category level in the fair value hierarchy is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Certain financial assets are not carried at fair value on a recurring basis, including investments such as mortgage loans, limited partnership interests, bank loans and policy loans. Accordingly, such investments are only included in the fair value hierarchy disclosure when the investment is subject to remeasurement at fair value after initial recognition and the resulting remeasurement is reflected in the consolidated financial statements. In addition, equity options embedded in fixed income securities are not disclosed in the hierarchy with free-standing derivatives as the embedded derivatives are presented with the host contract in fixed income securities.

SUMMARY OF SIGNIFICANT VALUATION TECHNIQUES FOR FINANCIAL ASSETS AND FINANCIAL LIABILITIES ON A RECURRING BASIS

LEVEL 1 MEASUREMENTS

- FIXED INCOME SECURITIES: U.S. treasuries are in Level 1 and valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.
- EQUITY SECURITIES: Comprise actively traded, exchange-listed U.S. and international equity securities. Valuation is based on unadjusted quoted prices for identical assets in active markets that the Company can access.
- SHORT-TERM: Comprise actively traded money market funds that have daily quoted net asset values for identical assets that the Company can access.
- SEPARATE ACCOUNT ASSETS: Comprise actively traded mutual funds that have daily quoted net asset values for identical assets that the Company can access. Net asset values for the actively traded mutual funds in which the separate account assets are invested are obtained daily from the fund managers.

LEVEL 2 MEASUREMENTS

- FIXED INCOME SECURITIES:
CORPORATE, INCLUDING PRIVATELY PLACED: Valued based on inputs including quoted prices for identical or similar assets in markets that are not active. Also includes privately placed securities which have market-observable external ratings from independent third party rating agencies.

MUNICIPAL: Externally rated municipals are valued based on inputs including quoted prices for identical or similar assets in markets that are not active. Included in municipals are auction rate securities ("ARS") other than those backed by student loans. ARS backed by student loans are included in Level 3.

U.S. GOVERNMENT AND AGENCIES: Valued based on inputs including quoted prices for identical or similar assets in markets that are not active.

COMMERCIAL MORTGAGE-BACKED SECURITIES ("CMBS"): Valuation is principally based on inputs including quoted prices for identical or similar assets in markets that are not active.

PREFERRED STOCK; MORTGAGE-BACKED SECURITIES ("MBS"); FOREIGN GOVERNMENT; ASSET-BACKED SECURITIES ("ABS") - CREDIT CARD: Valued based on inputs including quoted prices for identical or similar assets in markets that are not active.

- EQUITY SECURITIES: Valued based on inputs including quoted prices for identical or similar assets in markets that are not active.
- SHORT-TERM: Commercial paper and other short-term investments are valued based on quoted prices for identical or similar assets in markets that are not active or amortized cost.
- OTHER INVESTMENTS: Free-standing exchange listed derivatives that are not actively traded are valued based on quoted prices for identical instruments in markets that are not active.

Over-the-counter ("OTC") derivatives, including interest rate swaps, foreign currency swaps, foreign exchange forward contracts, and certain credit default swaps, are valued using models that rely on inputs such as interest rate yield curves, currency rates and adjustment for counterparty credit risks that are observable for substantially the full term of the contract. The valuation techniques underlying the models are widely accepted in the financial services industry and do not involve significant judgment.

- CONTRACTHOLDER FUNDS: Derivatives embedded in certain annuity contracts are valued based on internal models that rely on inputs such as interest rate yield curves and equity index volatility assumptions that are market observable for substantially the full term of the contract. The valuation techniques are widely accepted in the financial services industry and do not include significant judgment.

LEVEL 3 MEASUREMENTS

- FIXED INCOME SECURITIES:

CORPORATE: Valued based on non-binding broker quotes and are categorized as Level 3.

CORPORATE PRIVATELY PLACED: Valued based on non-binding broker quotes and models that are widely accepted in the financial services industry and use internally assigned credit ratings as inputs and instrument specific inputs. Instrument specific inputs used in internal fair value determinations include coupon rate, coupon type, weighted average life, sector of the issuer and call provisions. Privately placed securities are categorized as Level 3 as a result of the significance of non-market observable inputs. The internally modeled securities are valued based on internal ratings, which are not observable in the market. Multiple internal ratings comprise a National Association of Insurance Commissioners ("NAIC") rating category and when used in the internal model provide a more refined determination of fair value. The Company's internal ratings are primarily consistent with the NAIC ratings which are generally updated annually.

MUNICIPAL: ARS primarily backed by student loans that have become illiquid due to failures in the auction market and municipal bonds that are not rated by third party credit rating agencies but are generally rated by the NAIC are included in Level 3. ARS backed by student loans are valued based on a discounted cash flow model with certain inputs to the valuation model that are significant to the valuation, but are not market observable, including estimates of future coupon rates if auction failures continue, maturity assumptions, and illiquidity premium. Non-rated municipal bonds are valued based on valuation models that are widely accepted in the financial services industry and require projections of future cash flows that are not market-observable, and are categorized as Level 3 as a result of the significance of non-market

observable inputs.

ABS RESIDENTIAL MORTGAGE-BACKED SECURITIES ("ABS RMBS"); ALT-A RESIDENTIAL MORTGAGE-BACKED SECURITIES ("ALT-A"): ABS RMBS and Alt-A are principally valued based on inputs including quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

fair value measurements. Certain ABS RMBS and Alt-A are valued based on non-binding broker quotes. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, all ABS RMBS and Alt-A are categorized as Level 3.

OTHER COLLATERALIZED DEBT OBLIGATIONS ("CDO"); ABS COLLATERALIZED DEBT OBLIGATIONS ("ABS CDO"): Valued based on non-binding broker quotes received from brokers who are familiar with the investments. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, all collateralized loan obligations ("CLO"), ABS CDO, and synthetic collateralized debt obligations are categorized as Level 3.

CMBS; COMMERCIAL REAL ESTATE COLLATERALIZED DEBT OBLIGATIONS ("CRE CDO"): CRE CDO, which are reported as CMBS, and other CMBS, are either valued based on non-binding broker quotes or based on inputs including quoted prices for identical or similar assets in markets that exhibit less liquidity relative to those markets supporting Level 2 fair value measurements. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, certain CMBS are categorized as Level 3.

ABS - CREDIT CARD, AUTO AND STUDENT LOANS: Valued based on inputs including quoted prices for identical or similar assets in markets that are not active. Due to the reduced availability of actual market prices or relevant observable inputs as a result of the decrease in liquidity that has been experienced in the market for these securities, they are categorized as Level 3.

- OTHER INVESTMENTS: Certain free-standing OTC derivatives, such as caps, floors, certain credit default swaps and OTC options (including swaptions), are valued using valuation models that are widely accepted in the financial services industry. Inputs include non-market observable inputs such as volatility assumptions that are significant to the valuation of the instruments.
- CONTRACTHOLDER FUNDS: Derivatives embedded in annuity contracts are valued internally using models widely accepted in the financial services industry that determine a single best estimate of fair value for the embedded derivatives within a block of contractholder liabilities. The models use stochastically determined cash flows based on the contractual elements of embedded derivatives and other applicable market data. These are categorized as Level 3 as a result of the significance of non-market observable inputs.

FINANCIAL ASSETS AND FINANCIAL LIABILITIES ON A NON-RECURRING BASIS

Mortgage loans and other investments written-down to fair value in connection with recognizing other-than-temporary impairments are valued using valuation models that are widely accepted in the financial services industry. Inputs to the valuation models include non-market observable inputs such as credit spreads. Limited partnership interests written-down to fair value in connection with recognizing other-than-temporary impairments are valued using net asset values and other sources. At December 31, 2008, mortgage loans, limited partnership interests and other investments with a fair value of \$244 million were included in the fair value hierarchy in Level 3, since they were subject to remeasurement at fair value at December 31, 2008.

FAIR VALUE MEASUREMENT PRIOR TO ADOPTION OF SFAS NO. 157

Prior to the adoption of SFAS No. 157 on January 1, 2008, the fair value of fixed income securities was based upon observable market quotations, other market observable data or was derived from such quotations and market observable data. The fair value of privately placed fixed income securities was generally based on widely accepted pricing valuation models, which were developed

internally. The valuation models used security specific information such as the credit rating of the issuer, industry sector of the issuer, maturity, estimated duration, call provisions, sinking fund requirements, coupon rate, quoted market prices of comparable securities and estimated liquidity premiums to determine the overall spread for the specific security.

DERIVATIVE AND EMBEDDED DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments include interest rate swaps, credit default swaps, futures (interest rate and equity), options (including swaptions), interest rate caps and floors, warrants, forward contracts to hedge foreign currency risks and certain investment risk transfer reinsurance agreements. Derivatives that are required to be separated from the host instrument and accounted for as derivative financial instruments ("subject to bifurcation") are embedded in convertible and equity-indexed fixed income securities, equity-indexed life and annuity contracts, reinsured variable annuity contracts, and certain funding agreements (see Note 7).

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All derivatives are accounted for on a fair value basis and reported as other investments, other assets, other liabilities and accrued expenses or contractholder funds. Embedded derivative instruments subject to bifurcation are also accounted for on a fair value basis and are reported together with the host contract. The change in the fair value of derivatives embedded in certain fixed income securities and subject to bifurcation is reported in realized capital gains and losses. The change in the fair value of derivatives embedded in liabilities and subject to bifurcation is reported in contract benefits, interest credited to contractholder funds or realized capital gains and losses. Cash flows from embedded derivatives requiring bifurcation and derivatives receiving hedge accounting are reported consistently with the host contracts and hedged risks, respectively, within the Consolidated Statements of Cash Flows. Cash flows from other derivatives are reported in cash flows from investing activities within the Consolidated Statements of Cash Flows.

When derivatives meet specific criteria, they may be designated as accounting hedges and accounted for as fair value, cash flow, foreign currency fair value or foreign currency cash flow hedges. The hedged item may be either all or a specific portion of a recognized asset, liability or an unrecognized firm commitment attributable to a particular risk for fair value hedges. At the inception of the hedge, the Company formally documents the hedging relationship and risk management objective and strategy. The documentation identifies the hedging instrument, the hedged item, the nature of the risk being hedged and the methodology used to assess the effectiveness of the hedging instrument in offsetting the exposure to changes in the hedged item's fair value attributable to the hedged risk. In the case of a cash flow hedge, this documentation includes the exposure to changes in the variability in cash flows attributable to the hedged risk. The Company does not exclude any component of the change in fair value of the hedging instrument from the effectiveness assessment. At each reporting date, the Company confirms that the hedging instrument continues to be highly effective in offsetting the hedged risk. Ineffectiveness in fair value hedges and cash flow hedges is reported in realized capital gains and losses. The hedge ineffectiveness reported in realized capital gains and losses amounted to losses of \$4 million, \$13 million and \$7 million in 2008, 2007 and 2006, respectively.

FAIR VALUE HEDGES The Company designates certain of its interest rate and foreign currency swap contracts and certain investment risk transfer reinsurance agreements as fair value hedges when the hedging instrument is highly effective in offsetting the risk of changes in the fair value of the hedged item.

For hedging instruments used in fair value hedges, when the hedged items are investment assets or a portion thereof, the change in the fair value of the derivatives is reported in net investment income, together with the change in the fair value of the hedged items. The change in the fair value of hedging instruments used in fair value hedges of contractholder funds liabilities or a portion thereof is reported in interest credited to contractholder funds, together with the change in the fair value of the hedged items. Accrued periodic settlements on swaps are reported together with the changes in fair value of the swaps in net investment income or interest credited to contractholder funds. The amortized cost for fixed income securities, the carrying value for mortgage loans or the carrying value of the hedged liability is adjusted for the change in the fair value of the hedged risk.

CASH FLOW HEDGES The Company designates certain of its foreign currency swap contracts as cash flow hedges when the hedging instrument is highly effective in offsetting the exposure of variations in cash flows for the hedged risk that could affect net income. The Company's cash flow exposure may be

associated with an existing asset, liability or a forecasted transaction. Anticipated transactions must be probable of occurrence and their significant terms and specific characteristics must be identified.

For hedging instruments used in cash flow hedges, the changes in fair value of the derivatives representing the effective portion of the hedge are reported in accumulated other comprehensive income. Amounts are reclassified to net investment income or realized capital gains and losses as the hedged or forecasted transaction affects net income. Accrued periodic settlements on derivatives used in cash flow hedges are reported in net investment income. The amount reported in accumulated other comprehensive income for a hedged transaction is limited to the lesser of the cumulative gain or loss on the derivative less the amount reclassified to net income; or the cumulative gain or loss on the derivative needed to offset the cumulative change in the expected future cash flows on the hedged transaction from inception of the hedge less the derivative gain or loss previously reclassified from accumulated other comprehensive income to net income. If the Company expects at any time that the loss reported in accumulated other comprehensive income would lead to a net loss on the combination of the hedging instrument and the hedged transaction which may not be recoverable, a loss is recognized immediately in realized capital gains and losses. If an impairment loss is recognized on an asset or an additional obligation is incurred on a liability involved in a hedge

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transaction, any offsetting gain in accumulated other comprehensive income is reclassified and reported together with the impairment loss or recognition of the obligation.

TERMINATION OF HEDGE ACCOUNTING If, subsequent to entering into a hedge transaction, the derivative becomes ineffective (including if the hedged item is sold or otherwise extinguished, the occurrence of a hedged forecasted transaction is no longer probable, or the hedged asset becomes other-than-temporarily impaired), the Company may terminate the derivative position. The Company may also terminate derivative instruments or redesignate them as non-hedge as a result of other events or circumstances. If the derivative financial instrument is not terminated when a fair value hedge is no longer effective, the future gains and losses recognized on the derivative are reported in realized capital gains and losses. When a fair value hedge is no longer effective, is redesignated as non-hedge or when the derivative has been terminated, the fair value gain or loss on the hedged asset, liability or portion thereof which has already been recognized in income while the hedge was in place and used to adjust the amortized cost for fixed income securities, the carrying value for mortgage loans or the carrying amount for the liability, is amortized over the remaining life of the hedged asset, liability, or portion thereof, and reflected in net investment income or interest credited to contractholder funds beginning in the period that hedge accounting is no longer applied. If the hedged item in a fair value hedge is an asset which has become other-than-temporarily impaired, the adjustment made to the amortized cost for fixed income securities or the carrying value for mortgage loans is subject to the accounting policies applied to other-than-temporarily impaired assets.

When a derivative financial instrument used in a cash flow hedge of an existing asset or liability is no longer effective or is terminated, the gain or loss recognized on the derivative is reclassified from accumulated other comprehensive income to net income as the hedged risk impacts net income. If the derivative financial instrument is not terminated when a cash flow hedge is no longer effective, the future gains and losses recognized on the derivative are reported in realized capital gains and losses. When a derivative financial instrument used in a cash flow hedge of a forecasted transaction is terminated because the forecasted transaction is no longer probable, the gain or loss recognized on the derivative is immediately reclassified from accumulated other comprehensive income to realized capital gains and losses in the period that hedge accounting is no longer applied. If a cash flow hedge is no longer effective, the gain or loss recognized on the derivative during the period the hedge was effective is reclassified from accumulated other comprehensive income to net income as the remaining hedged item affects net income.

NON-HEDGE DERIVATIVE FINANCIAL INSTRUMENTS The Company also has certain derivatives that are used in interest rate, equity price and credit risk management strategies for which hedge accounting is not applied. These derivatives primarily consist of certain interest rate swap agreements, equity options and futures, financial futures contracts, interest rate cap and floor agreements, swaptions, foreign currency forward and option contracts and credit default swaps.

In addition to the use of credit default swaps for credit risk management strategies, the Company replicates fixed income securities using a combination

of a credit default swap and one or more highly rated fixed income securities to synthetically replicate the economic characteristics of one or more cash market securities. Fixed income securities are replicated when they are either unavailable in the cash market or are more economical to acquire in synthetic form.

Based upon the type of derivative instrument and strategy, the income statement effects of these derivatives are reported in a single line item with the results of the associated risk. Therefore, the derivatives' fair value gains and losses and accrued periodic settlements are recognized together in one of the following during the reporting period: net investment income, realized capital gains and losses, operating costs and expenses, contract benefits or interest credited to contractholder funds.

SECURITIES LOANED AND SECURITY REPURCHASE AND RESALE

The Company's business activities include securities lending transactions, securities sold under agreements to repurchase ("repurchase agreements"), and securities purchased under agreements to resell ("resale agreements"), which are used primarily to generate net investment income. The proceeds received from repurchase agreements also provide a source of liquidity. For repurchase agreements and securities lending transactions used to generate net investment income, the proceeds received are reinvested in short-term investments or fixed income securities. These transactions are short-term in nature, usually 30 days or less.

The Company receives cash collateral for securities loaned in an amount generally equal to 102% of the fair value of securities and records the related obligations to return the collateral in other liabilities and accrued

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expenses. The carrying value of these obligations approximates fair value because of their relatively short-term nature. The Company monitors the market value of securities loaned on a daily basis and obtains additional collateral as necessary under the terms of the agreements to mitigate counterparty credit risk. The Company maintains the right and ability to redeem the securities loaned on short notice. Substantially all of the Company's securities loaned are placed with large banks.

The Company's policy is to take possession or control of securities under resale agreements. Securities to be repurchased under repurchase agreements are the same, or substantially the same, as the securities transferred. The Company's obligations to return the funds received under repurchase agreements are carried at the amount at which the securities will subsequently be reacquired, including accrued interest, as specified in the respective agreements and are classified as other liabilities and accrued expenses. The carrying value of these obligations approximates fair value because of their relatively short-term nature.

RECOGNITION OF PREMIUM REVENUES AND CONTRACT CHARGES, AND RELATED BENEFITS AND INTEREST CREDITED

Traditional life insurance products consist principally of products with fixed and guaranteed premiums and benefits, primarily term and whole life insurance products. Premiums from these products are recognized as revenue when due from policyholders. Benefits are reflected in contract benefits and recognized in relation to premiums, so that profits are recognized over the life of the policy.

Immediate annuities with life contingencies, including certain structured settlement annuities, provide insurance protection over a period that extends beyond the period during which premiums are collected. Premiums from these products are recognized as revenue when received at the inception of the contract. Benefits and expenses are recognized in relation to premiums. Profits from these policies come from investment income, which is recognized over the life of the contract.

Interest-sensitive life contracts, such as universal life and single premium life, are insurance contracts whose terms are not fixed and guaranteed. The terms that may be changed include premiums paid by the contractholder, interest credited to the contractholder account balance and contract charges assessed against the contractholder account balance. Premiums from these contracts are reported as contractholder fund deposits. Contract charges consist of fees assessed against the contractholder account balance for the cost of insurance (mortality risk), contract administration and early surrender. These contract charges are recognized as revenue when assessed against the contractholder account balance. Contract benefits include life-contingent

benefit payments in excess of the contractholder account balance.

Contracts that do not subject the Company to significant risk arising from mortality or morbidity are referred to as investment contracts. Fixed annuities, including market value adjusted annuities, equity-indexed annuities and immediate annuities without life contingencies, and funding agreements (primarily backing medium-term notes) are considered investment contracts. Consideration received for such contracts is reported as contractholder fund deposits. Contract charges for investment contracts consist of fees assessed against the contractholder account balance for maintenance, administration and surrender of the contract prior to contractually specified dates, and are recognized when assessed against the contractholder account balance.

Interest credited to contractholder funds represents interest accrued or paid on interest-sensitive life contracts and investment contracts. Crediting rates for certain fixed annuities and interest-sensitive life contracts are adjusted periodically by the Company to reflect current market conditions subject to contractually guaranteed minimum rates. Crediting rates for indexed annuities and indexed funding agreements are generally based on a specified interest rate index, such as LIBOR, or an equity index, such as the Standard & Poor's ("S&P") 500 Index. Interest credited also includes amortization of DSI expenses. DSI is amortized into interest credited using the same method used to amortize DAC.

Contract charges for variable life and variable annuity products consist of fees assessed against the contractholder account values for contract maintenance, administration, mortality, expense and early surrender. Contract benefits incurred include guaranteed minimum death, income, withdrawal and accumulation benefits. Subsequent to the Company's disposal of substantially all of its variable annuity business through reinsurance agreements with Prudential in 2006 (see Note 3), the contract charges and contract benefits related thereto are reported net of reinsurance ceded.

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DEFERRED POLICY ACQUISITION AND SALES INDUCEMENT COSTS

Costs that vary with and are primarily related to acquiring life insurance and investment contracts are deferred and recorded as DAC. These costs are principally agents' and brokers' remuneration, and certain underwriting expenses. DSI costs, which are deferred and recorded as other assets, relate to sales inducements offered on sales to new customers, principally on annuities and primarily in the form of additional credits to the customer's account value or enhancements to interest credited for a specified period, which are in excess of the rates currently being credited to similar contracts without sales inducements. All other acquisition costs are expensed as incurred and included in operating costs and expenses on the Consolidated Statements of Operations and Comprehensive Income. Future investment income is considered in determining the recoverability of DAC. Amortization of DAC is included in amortization of deferred policy acquisition costs on the Consolidated Statements of Operations and Comprehensive Income and is described in more detail below. DSI is amortized to income using the same methodology and assumptions as DAC and is included in interest credited to contractholder funds on the Consolidated Statements of Operations and Comprehensive Income. DAC and DSI are periodically reviewed for recoverability and adjusted if necessary.

For traditional life insurance, DAC is amortized over the premium paying period of the related policies in proportion to the estimated revenues on such business. Assumptions used in the amortization of DAC and reserve calculations are established at the time the policy is issued and are generally not revised during the life of the policy. Any deviations from projected business in force resulting from actual policy terminations differing from expected levels and any estimated premium deficiencies may result in a change to the rate of amortization in the period such events occur. Generally, the amortization periods for these policies approximates the estimated lives of the policies.

For interest-sensitive life, annuities and other investment contracts, DAC and DSI are amortized in proportion to the incidence of the total present value of gross profits, which includes both actual historical gross profits ("AGP") and estimated future gross profits ("EGP") expected to be earned over the estimated lives of the contracts. The amortization is net of interest on the prior period DAC balance and uses rates established at the inception of the contracts. Actual amortization periods generally range from 15-30 years; however, incorporating estimates of customer surrender rates, partial withdrawals and deaths generally results in the majority of the DAC being amortized during the surrender charge period. The rate of amortization during this term is matched to the recognition pattern of total gross profits.

AGP and EGP consist primarily of the following components: contract charges for the cost of insurance less mortality costs and other benefits; investment income and realized capital gains and losses less interest credited; and surrender and other contract charges less maintenance expenses. The principal assumptions for determining the amount of EGP are investment returns, including capital gains and losses on assets supporting contract liabilities, interest crediting rates to contractholders, and the effects of persistency, mortality, expenses and hedges, if applicable.

Changes in the amount or timing of EGP result in adjustments to the cumulative amortization of DAC and DSI. All such adjustments are reflected in the current results of operations.

The Company performs quarterly reviews of DAC and DSI recoverability for interest-sensitive life, annuities and other investment contracts in the aggregate using current assumptions. If a change in the amount of EGP is significant, it could result in the unamortized DAC and DSI not being recoverable, resulting in a charge which is included as a component of amortization of deferred policy acquisition costs or interest credited to contractholder funds, respectively, on the Consolidated Statements of Operations and Comprehensive Income.

Any amortization of DAC or DSI that would result from changes in unrealized capital gains or losses had those gains or losses actually been realized during the reporting period is recorded net of tax in other comprehensive income. Recapitalization of DAC and DSI is limited to the originally deferred costs plus interest.

Customers of the Company may exchange one insurance policy or investment contract for another offered by the Company, or make modifications to an existing life or investment contract issued by the Company. These transactions are identified as internal replacements for accounting purposes. Internal replacement transactions that are determined to result in replacement contracts that are substantially unchanged from the replaced contracts are accounted for as continuations of the replaced contracts. Unamortized DAC and DSI related to the replaced contract continue to be deferred and amortized in connection with the replacement contract. For interest-sensitive life insurance and investment contracts, the EGP of the replacement contract is treated as a revision to the EGP of the replaced contract in the determination of amortization of DAC and DSI. For traditional life insurance policies, any

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changes to unamortized DAC and benefit reserves that result from the replacement contract are treated as prospective revisions. Any costs associated with the issuance of the replacement contract are characterized as maintenance costs and expensed as incurred.

Internal replacement transactions that are determined to result in a substantial change to the replaced contracts are accounted for as an extinguishment of the replaced contracts, and any unamortized DAC and DSI related to the replaced contracts are eliminated with a corresponding charge to the Consolidated Statements of Operations and Comprehensive Income.

The costs assigned to the right to receive future cash flows from certain business purchased from other insurers are also classified as DAC in the Consolidated Statements of Financial Position. The costs capitalized represent the present value of future profits expected to be earned over the lives of the contracts acquired. These costs are amortized as profits emerge over the lives of the acquired business and are periodically evaluated for recoverability. The present value of future profits was \$19 million and \$21 million at December 31, 2008 and 2007, respectively. Amortization expense on the present value of future profits was \$5 million, \$5 million and \$6 million for the years ended December 31, 2008, 2007 and 2006, respectively.

REINSURANCE

In the normal course of business, the Company seeks to limit aggregate and single exposure to losses on large risks by purchasing reinsurance (see Note 9). The Company has also used reinsurance to effect the acquisition or disposition of certain blocks of business. The amounts reported in the Consolidated Statements of Financial Position as reinsurance recoverables include amounts billed to reinsurers on losses paid as well as estimates of amounts expected to be recovered from reinsurers on insurance liabilities and contractholder funds that have not yet been paid. Reinsurance recoverables on unpaid losses are estimated based upon assumptions consistent with those used in establishing the liabilities related to the underlying reinsured contracts. Insurance liabilities are reported gross of reinsurance recoverables. Reinsurance premiums are

generally reflected in income in a manner consistent with the recognition of premiums on the reinsured contracts. Reinsurance does not extinguish the Company's primary liability under the policies written. Therefore, the Company regularly evaluates the financial condition of its reinsurers including their activities with respect to claim settlement practices and commutations, and establishes allowances for uncollectible reinsurance recoverables as appropriate.

GOODWILL

Goodwill represents the excess of amounts paid for acquiring businesses over the fair value of the net assets acquired. The goodwill balance was \$5 million at both December 31, 2008 and 2007. The Company annually evaluates goodwill for impairment using both a discounted cash flow analysis and a trading multiple analysis, which are widely accepted valuation techniques to estimate the fair value of its reporting units. The Company also reviews its goodwill for impairment whenever events or changes in circumstances indicate that it is more likely than not that the carrying amount of goodwill may exceed its implied fair value. Goodwill impairment evaluations indicated no impairment at December 31, 2008 or 2007.

INCOME TAXES

The income tax provision is calculated under the liability method. Deferred tax assets and liabilities are recorded based on the difference between the financial statement and tax bases of assets and liabilities at the enacted tax rates. The principal assets and liabilities giving rise to such differences are unrealized capital gains and losses on certain investments, differences in tax bases of investments, insurance reserves and DAC. A deferred tax asset valuation allowance is established when there is uncertainty that such assets would be realized (see Note 12).

RESERVE FOR LIFE-CONTINGENT CONTRACT BENEFITS

The reserve for life-contingent contract benefits payable under insurance policies, including traditional life insurance, life-contingent immediate annuities and voluntary health products, is computed on the basis of long-term actuarial assumptions of future investment yields, mortality, morbidity, policy terminations and expenses (see Note 8). These assumptions, which for traditional life insurance are applied using the net level premium method, include provisions for adverse deviation and generally vary by characteristics such as type of coverage, year of issue and policy duration. To the extent that unrealized gains on fixed income securities would result in a premium deficiency had those gains actually been realized, the related increase in reserves for certain immediate annuities with life contingencies is recorded net of tax as a reduction of unrealized net capital gains included in accumulated other comprehensive income.

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CONTRACTHOLDER FUNDS

Contractholder funds represent interest-bearing liabilities arising from the sale of products, such as interest-sensitive life, fixed annuities and funding agreements. Contractholder funds are comprised primarily of deposits received and interest credited to the benefit of the contractholder less surrenders and withdrawals, mortality charges and administrative expenses (see Note 8). Contractholder funds also include reserves for secondary guarantees on interest-sensitive life insurance and certain fixed annuity contracts and reserves for certain guarantees on reinsured variable annuity contracts.

SEPARATE ACCOUNTS

Separate accounts assets are carried at fair value. The assets of the separate accounts are legally segregated and available only to settle separate account contract obligations. Separate accounts liabilities represent the contractholders' claims to the related assets and are carried at an amount equal to the separate accounts assets. Investment income and realized capital gains and losses of the separate accounts accrue directly to the contractholders and therefore, are not included in the Company's Consolidated Statements of Operations and Comprehensive Income. Deposits to and surrenders and withdrawals from the separate accounts are reflected in separate accounts liabilities and are not included in consolidated cash flows.

Absent any contract provision wherein the Company provides a guarantee, variable annuity and variable life insurance contractholders bear the investment risk that the separate accounts' funds may not meet their stated investment objectives. Substantially all of the Company's variable annuity business is

reinsured to Prudential beginning in 2006.

OFF-BALANCE-SHEET FINANCIAL INSTRUMENTS

Commitments to invest, commitments to purchase private placement securities, commitments to extend mortgage loans and financial guarantees have off-balance-sheet risk because their contractual amounts are not recorded in the Company's Consolidated Statements of Financial Position (see Note 7 and Note 11).

ADOPTED ACCOUNTING STANDARDS

SECURITIES AND EXCHANGE COMMISSION ("SEC") STAFF ACCOUNTING BULLETIN NO. 109, WRITTEN LOAN COMMITMENTS THAT ARE RECORDED AT FAIR VALUE THROUGH EARNINGS ("SAB 109")

In October 2007, the SEC issued SAB 109, a replacement of SAB 105, "Application of Accounting Principles to Loan Commitments". SAB 109 is applicable to both loan commitments accounted for under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"), and other loan commitments for which the issuer elects fair value accounting under SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities". SAB 109 states that the expected net future cash flows related to the servicing of a loan should be included in the fair value measurement of a loan commitment accounted for at fair value through earnings. The expected net future cash flows associated with loan servicing should be determined in accordance with the guidance in SFAS No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities", as amended by SFAS No. 156, "Accounting for Servicing of Financial Assets". SAB 109 should be applied on a prospective basis to loan commitments accounted for under SFAS No. 133 that were issued or modified in fiscal quarters beginning after December 15, 2007. Earlier adoption was not permitted. The adoption of SAB 109 did not have a material impact on the Company's results of operations or financial position.

SFAS NO. 157, FAIR VALUE MEASUREMENTS ("SFAS NO. 157")

In September 2006, the Financial Accounting Standards Board ("FASB") issued SFAS No. 157, which redefines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establishes a framework for measuring fair value in GAAP, and expands disclosures about fair value measurements. SFAS No. 157 establishes a three-level hierarchy for fair value measurements based upon the nature of the inputs to the valuation of an asset or liability. SFAS No. 157 applies where other accounting pronouncements require or permit fair value measurements. In February 2008, the FASB issued FASB Staff Position No. 157-2, "Effective Date of FASB Statement No. 157" ("FSP FAS 157-2"), which permits the deferral of the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008 for all non-financial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis. The Company adopted the provisions of SFAS No. 157 for financial assets and financial liabilities recognized or disclosed at fair value on a recurring or non-recurring basis as

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of January 1, 2008. Consistent with the provisions of FSP FAS 157-2, the Company decided to defer the adoption of SFAS No. 157 for non-financial assets and liabilities measured at fair value on a non-recurring basis until January 1, 2009. In October 2008, the FASB issued FASB Staff Position No. FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active" ("FSP FAS 157-3"), which clarifies the application of SFAS 157 in a market that is not active. The Company adopted the provisions of FSP FAS 157-3 as of September 30, 2008. The adoption of SFAS No. 157 and FSP FAS 157-3 did not have a material effect on the Company's results of operations or financial position (see Note 7).

SFAS NO. 159, THE FAIR VALUE OPTION FOR FINANCIAL ASSETS AND FINANCIAL LIABILITIES - INCLUDING AN AMENDMENT OF FASB STATEMENT NO. 115 ("SFAS NO. 159")

In February 2007, the FASB issued SFAS No. 159 which provides reporting entities, on an ongoing basis, an option to report selected financial assets, including investment securities, and financial liabilities, including most insurance contracts, at fair value through earnings. SFAS No. 159 establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement alternatives for similar types of financial assets and liabilities. The standard also requires additional information to aid financial statement users' understanding of the impacts of a

reporting entity's decision to use fair value on its earnings and requires entities to display, on the face of the statement of financial position, the fair value of those assets and liabilities for which the reporting entity has chosen to measure at fair value. SFAS No. 159 was effective as of the beginning of a reporting entity's first fiscal year beginning after November 15, 2007. The Company did not apply the fair value option to any existing financial assets or liabilities as of January 1, 2008 and did not elect to apply the option prospectively to any financial assets or liabilities acquired during 2008. Consequently, the adoption of SFAS No. 159 had no impact on the Company's results of operations or financial position.

FASB STAFF POSITION NO. FIN 39-1, AMENDMENT OF FASB INTERPRETATION NO. 39 ("FSP FIN 39-1")

In April 2007, the FASB issued FSP FIN 39-1, which amends FASB Interpretation No. 39, "Offsetting of Amounts Related to Certain Contracts". FSP FIN 39-1 replaces the terms "conditional contracts" and "exchange contracts" with the term "derivative instruments" and requires a reporting entity to offset fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral against fair value amounts recognized for derivative instruments executed with the same counterparty under the same master netting arrangement that have been offset in the statement of financial position. FSP FIN 39-1 was effective for fiscal years beginning after November 15, 2007, with early adoption permitted. The adoption of FSP FIN 39-1 did not have a material impact on the Company's results of operations or financial position.

STATEMENT OF POSITION 05-1, ACCOUNTING BY INSURANCE ENTERPRISES FOR DEFERRED ACQUISITION COSTS IN CONNECTION WITH MODIFICATIONS OR EXCHANGES OF INSURANCE CONTRACTS ("SOP 05-1")

In October 2005, the American Institute of Certified Public Accountants ("AICPA") issued SOP 05-1. SOP 05-1 provides accounting guidance for DAC associated with internal replacements of insurance and investment contracts other than those set forth in SFAS No. 97, "Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments". SOP 05-1 defines an internal replacement as a modification in product benefits, features, rights or coverages that occurs through the exchange of an existing contract for a new contract, or by amendment, endorsement or rider to an existing contract, or by the election of a feature or coverage within an existing contract. The Company adopted the provisions of SOP 05-1 on January 1, 2007 for internal replacements occurring in fiscal years beginning after December 15, 2006. The adoption resulted in an \$8 million after-tax reduction to retained income to reflect the impact on EGP from the changes in accounting for certain costs associated with contract continuations that no longer qualify for deferral under SOP 05-1 and a reduction of DAC and DSI balances of \$13 million pre-tax as of January 1, 2007.

SFAS NO. 155, ACCOUNTING FOR CERTAIN HYBRID FINANCIAL INSTRUMENTS - AN AMENDMENT OF FASB STATEMENTS NO. 133 AND 140 ("SFAS NO. 155")

In February 2006, the FASB issued SFAS No. 155, which permits the fair value remeasurement at the date of adoption of any hybrid financial instrument containing an embedded derivative that otherwise would require bifurcation under paragraph 12 or 13 of SFAS No. 133; clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS No. 133; establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or hybrid financial instruments that contain embedded derivatives requiring bifurcation; and clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives. The Company adopted the provisions of SFAS No. 155 on January 1,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2007, which were effective for all financial instruments acquired, issued or subject to a remeasurement event occurring after the beginning of the first fiscal year beginning after September 15, 2006. The Company elected not to remeasure existing hybrid financial instruments that contained embedded derivatives requiring bifurcation at the date of adoption pursuant to paragraph 12 or 13 of SFAS No. 133. The adoption of SFAS No. 155 did not have a material effect on the results of operations or financial position of the Company.

FASB INTERPRETATION NO. 48, ACCOUNTING FOR UNCERTAINTY IN INCOME TAXES - AN INTERPRETATION OF FASB STATEMENT NO. 109 AND FASB STAFF POSITION NO. FIN 48-1, DEFINITION OF SETTLEMENT IN FASB INTERPRETATION NO. 48 (COLLECTIVELY "FIN 48")

The FASB issued the interpretation in July 2006 and the related staff

position in May 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes". FIN 48 requires an entity to recognize the tax benefit of uncertain tax positions only when it is more likely than not, based on the position's technical merits, that the position would be sustained upon examination by the respective taxing authorities. The tax benefit is measured as the largest benefit that is more than fifty-percent likely of being realized upon final settlement with the respective taxing authorities. On January 1, 2007, the Company adopted the provisions of FIN 48, which were effective for fiscal years beginning after December 15, 2006. No cumulative effect of a change in accounting principle or adjustment to the liability for unrecognized tax benefits was recognized as a result of the adoption of FIN 48. Accordingly, the adoption of FIN 48 did not have an effect on the results of operations or financial position of the Company (see Note 12).

SEC STAFF ACCOUNTING BULLETIN NO. 108, CONSIDERING THE EFFECTS OF PRIOR YEAR MISSTATEMENTS WHEN QUANTIFYING MISSTATEMENTS IN CURRENT YEAR FINANCIAL STATEMENTS ("SAB 108")

In September 2006, the SEC issued SAB 108 to eliminate the diversity of practice in the way misstatements are quantified for purposes of assessing their materiality in financial statements. SAB 108 was intended to eliminate the potential build up of improper amounts on the balance sheet due to the limitations of certain methods of assessing materiality previously utilized by some reporting entities. SAB 108 established a single quantification framework wherein the significance determination is based on the effects of the misstatements on each of the financial statements as well as the related financial statement disclosures. On December 31, 2006, the Company adopted the provisions of SAB 108 which were effective for the first fiscal year ending after November 15, 2006. The adoption of SAB 108 did not have any effect on the results of operations or financial position of the Company.

FASB STAFF POSITION NO. FAS 115-1/124-1, THE MEANING OF OTHER-THAN-TEMPORARY IMPAIRMENT AND ITS APPLICATION TO CERTAIN INVESTMENTS ("FSP FAS 115-1/124-1")

FSP FAS 115-1/124-1 nullified the guidance in paragraphs 10-18 of Emerging Issues Task Force Issue 03-1, "The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments" and references existing other-than-temporary impairment guidance. FSP FAS 115-1/124-1 clarifies that an investor should recognize an impairment loss no later than when the impairment is deemed other-than-temporary, even if a decision to sell the security has not been made, and also provides guidance on the subsequent income recognition for impaired debt securities. The Company adopted FSP FAS 115-1/124-1 as of January 1, 2006 on a prospective basis. The effects of adoption did not have a material effect on the results of operations or financial position of the Company.

SFAS NO. 154, ACCOUNTING CHANGES AND ERROR CORRECTIONS - A REPLACEMENT OF APB OPINION NO. 20 AND FASB STATEMENT NO. 3 ("SFAS NO. 154")

SFAS No. 154 replaced Accounting Principles Board ("APB") Opinion No. 20, "Accounting Changes", and SFAS No. 3, "Reporting Accounting Changes in Interim Financial Statements". SFAS No. 154 requires retrospective application to prior periods' financial statements for changes in accounting principle, unless determination of either the period specific effects or the cumulative effect of the change is impracticable or otherwise not required. The Company adopted SFAS No. 154 on January 1, 2006. The adoption of SFAS No. 154 did not have any effect on the results of operations or financial position of the Company.

FSP NO. FAS 133-1 AND FIN 45-4, DISCLOSURES ABOUT CREDIT DERIVATIVES AND CERTAIN GUARANTEES: AN AMENDMENT OF FASB STATEMENT NO. 133 AND FASB INTERPRETATION NO. 45; AND CLARIFICATION OF THE EFFECTIVE DATE OF FASB STATEMENT NO. 161 ("FSP FAS 133-1 AND FIN 45-4")

In September 2008, the FASB issued FSP FAS 133-1 and FIN 45-4, which amends SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" ("SFAS No. 133"), and FIN 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45"), to

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both enhance and synchronize the disclosure requirements of the two statements with respect to the potential for adverse effects of changes in credit risk on the financial statements of the sellers of credit derivatives and certain guarantees. SFAS No. 133 was amended to require disclosures by sellers of credit derivatives, including credit derivatives embedded in a hybrid instrument. FIN 45 was amended to require an additional disclosure about the current status of the payment/performance risk of a guarantee. The FSP clarifies the FASB's intent

that the disclosures required by SFAS No. 161 should be provided for any reporting period (annual or quarterly interim) beginning after November 15, 2008. The provisions of this FASB staff position that amend SFAS No. 133 and FIN 45 are effective for reporting periods ending after November 15, 2008, and the provisions that clarify the effective date SFAS No. 161 are effective upon the adoption of that statement; therefore, the disclosure requirements, which have no impact to the Company's results of operations or financial position, were adopted at December 31, 2008.

FSP NO. EITF 99-20-1, AMENDMENTS TO THE IMPAIRMENT GUIDANCE OF EITF ISSUE NO. 99-20 ("FSP EITF 99-20-1")

In January 2009, the FASB issued FSP EITF 99-20-1, which amends FASB Emerging Issues Task Force ("EITF") No. 99-20 "Recognition of Interest Income and Impairment on Purchased Beneficial Interest and Beneficial Interests That Continue to Be Held by a Transferor or in Securitized Financial Assets," ("EITF 99-20"), to align the impairment guidance in EITF 99-20 with the impairment guidance and related implementation guidance in SFAS No. 115 "Accounting for Certain Investments in Debt and Equity Securities". The provisions of this FASB staff position are effective for reporting periods ending after December 15, 2008. The adoption of FSP EITF 99-20-1 did not have a material effect on the results of operations or financial position of the Company.

PENDING ACCOUNTING STANDARDS

SFAS NO. 141(R), BUSINESS COMBINATIONS ("SFAS NO. 141R")

In December 2007, the FASB issued SFAS No. 141R which replaces SFAS No. 141, "Business Combinations" ("SFAS No. 141"). Among other things, SFAS No. 141R broadens the scope of SFAS No. 141 to include all transactions where an acquirer obtains control of one or more other businesses; retains the guidance to recognize intangible assets separately from goodwill; requires, with limited exceptions, that all assets acquired and liabilities assumed, including certain of those that arise from contractual contingencies, be measured at their acquisition date fair values; requires most acquisition and restructuring-related costs to be expensed as incurred; requires that step acquisitions, once control is acquired, be recorded at the full amounts of the fair values of the identifiable assets, liabilities and the noncontrolling interest in the acquiree; and replaces the reduction of asset values and recognition of negative goodwill with a requirement to recognize a gain in earnings. The provisions of SFAS No. 141R are effective for fiscal years beginning after December 15, 2008 and are to be applied prospectively only. Early adoption is not permitted. The Company will apply the provisions of SFAS No. 141R as required when effective.

SFAS NO. 160, NONCONTROLLING INTERESTS IN CONSOLIDATED FINANCIAL STATEMENTS - AN AMENDMENT OF ARB NO. 51 ("SFAS NO. 160")

In December 2007, the FASB issued SFAS No. 160 which clarifies that a noncontrolling interest in a subsidiary is that portion of the subsidiary's equity that is attributable to owners of the subsidiary other than its parent or parent's affiliates. Noncontrolling interests are required to be reported as equity in the consolidated financial statements and as such net income will include amounts attributable to both the parent and the noncontrolling interest with disclosure of the amounts attributable to each on the face of the Consolidated Statements of Operations and Comprehensive Income. SFAS No. 160 requires that all changes in a parent's ownership interest in a subsidiary when control of the subsidiary is retained, be accounted for as equity transactions. In contrast, when control over a subsidiary is relinquished and the subsidiary is deconsolidated, SFAS No. 160 requires a parent to recognize a gain or loss in net income as well as provide certain associated expanded disclosures. SFAS No. 160 is effective as of the beginning of a reporting entity's first fiscal year beginning after December 15, 2008. Early adoption is prohibited. SFAS No. 160 requires prospective application as of the beginning of the fiscal year in which the standard is initially applied, except for the presentation and disclosure requirements which are to be applied retrospectively for all periods presented. The adoption of SFAS No. 160 is not expected to have a material effect on the Company's results of operations or financial position.

SFAS NO. 161, DISCLOSURES ABOUT DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES - AN AMENDMENT OF FASB STATEMENT NO. 133 ("SFAS NO. 161")

In March 2008, the FASB issued SFAS No. 161, which amends and expands the disclosure requirements for derivatives currently accounted for in accordance with SFAS No. 133. The new disclosures are designed to enhance the understanding of how and why an entity uses derivative instruments and how derivative instruments affect an

entity's financial position, results of operations, and cash flows. The standard requires, on a quarterly basis, quantitative disclosures about the potential cash outflows associated with the triggering of credit-related contingent features, if any; tabular disclosures about the classification and fair value amounts of derivative instruments reported in the statement of financial position; disclosure of the location and amount of gains and losses on derivative instruments reported in the statement of operations; and qualitative information about how and why an entity uses derivative instruments and how derivative instruments and related hedged items affect the entity's financial statements. SFAS No. 161 is effective for fiscal periods beginning after November 15, 2008, and is to be applied on a prospective basis only. SFAS No. 161 affects disclosures and therefore implementation will not impact the Company's results of operations or financial position.

3. DISPOSITIONS

VARIABLE ANNUITY BUSINESS

On June 1, 2006, in accordance with the terms of the definitive Master Transaction Agreement and related agreements (collectively the "Agreement") ALIC, its subsidiary, Allstate Life Insurance Company of New York ("ALNY"), and the Corporation completed the disposal through reinsurance of substantially all of the Company's variable annuity business to Prudential Financial, Inc. and its subsidiary, The Prudential Insurance Company of America (collectively "Prudential"). For Allstate, this disposal achieved the economic benefit of transferring to Prudential the future rights and obligations associated with this business.

The disposal was effected through reinsurance agreements (the "Reinsurance Agreements") which include both coinsurance and modified coinsurance provisions. Coinsurance and modified coinsurance provisions are commonly used in the reinsurance of variable annuities because variable annuities generally include both separate account and general account liabilities. When contractholders make a variable annuity deposit, they must choose how to allocate their account balances between a selection of variable-return mutual funds that must be held in a separate account and fixed-return funds held in the Company's general account. In addition, variable annuity contracts include various benefit guarantees that are general account obligations of the Company. The Reinsurance Agreements do not extinguish the Company's primary liability under the variable annuity contracts.

Variable annuity balances invested in variable-return mutual funds are held in separate accounts, which are legally segregated assets and available only to settle separate account contract obligations. Because the separate account assets must remain with the Company under insurance regulations, modified coinsurance is typically used when parties wish to transfer future economic benefits of such business. Under the modified coinsurance provisions, the separate account assets remain on the Company's Consolidated Statements of Financial Position, but the related results of operations are fully reinsured and presented net of reinsurance on the Consolidated Statements of Operations and Comprehensive Income.

The coinsurance provisions of the Reinsurance Agreements were used to transfer the future rights and obligations related to fixed-return fund options and benefit guarantees. \$1.37 billion of assets supporting general account liabilities have been transferred to Prudential, net of consideration, under the coinsurance reinsurance provisions as of the transaction closing date. General account liabilities of \$1.57 billion and \$1.26 billion as of December 31, 2008 and 2007, respectively, however, remain on the Consolidated Statements of Financial Position with a corresponding reinsurance recoverable.

For purposes of presentation in the Consolidated Statements of Cash Flows, the Company treated the reinsurance of substantially all the variable annuity business of ALIC and ALNY to Prudential as a disposition of operations, consistent with the substance of the transaction which was the disposition of a block of business accomplished through reinsurance. Accordingly, the net consideration transferred to Prudential of \$744 million (computed as \$1.37 billion of general account insurance liabilities transferred to Prudential on the closing date less consideration of \$628 million), the cost of hedging the ceding commission received from Prudential of \$69 million, pre-tax, and the costs of executing the transaction of \$13 million, pre-tax, were classified as a disposition of operations in the cash flows from investing activities section of the Consolidated Statements of Cash Flows.

Under the Agreement, ALIC, ALNY and the Corporation have indemnified Prudential for certain pre-closing contingent liabilities (including extra-contractual liabilities of ALIC and ALNY and liabilities specifically excluded from the transaction) that ALIC and ALNY have agreed to retain. In addition, ALIC, ALNY and the Corporation will indemnify Prudential for certain

post-closing liabilities that may arise from the acts of ALIC, ALNY and their agents, including in connection with ALIC's and ALNY's provision of transition services. The Reinsurance Agreements contain no limits or indemnifications with regard to insurance risk transfer, and transferred all of the future risks and responsibilities for performance on the underlying variable annuity contracts to Prudential, including

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those related to benefit guarantees, in accordance with the provisions of SFAS No. 113 "Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts".

The terms of the Agreement give Prudential the right to be the exclusive provider of its variable annuity products through the Allstate proprietary agency force for three years and a non-exclusive preferred provider for the following two years. During a transition period which ended May 2008, the Company continued to issue new variable annuity contracts, accept additional deposits on existing business from existing contractholders on behalf of Prudential and service the reinsured business while Prudential prepared for the migration of the business onto its servicing platform.

Pursuant to the Agreement, the final market-adjusted consideration was \$628 million. The disposal resulted in a gain of \$79 million pre-tax for ALIC, which was deferred as a result of the disposition being executed through reinsurance. The deferred gain is included as a component of other liabilities and accrued expenses on the Consolidated Statements of Financial Position, and is amortized to gain (loss) on disposition of operations on the Consolidated Statements of Operations and Comprehensive Income over the life of the reinsured business which is estimated to be approximately 18 years. For ALNY, the transaction resulted in a loss of \$9 million pre-tax. ALNY's reinsurance loss and other amounts related to the disposal of the business, including the initial costs and final market value settlements of the derivatives acquired by ALIC to economically hedge substantially all of the exposure related to market adjustments between the effective date of the Agreement and the closing of the transaction, transactional expenses incurred and amortization of ALIC's deferred reinsurance gain, were included as a component of gain (loss) on disposition of operations on the Consolidated Statements of Operations and Comprehensive Income and amounted to \$5 million, \$6 million and \$(61) million, after-tax during 2008, 2007 and 2006, respectively. Gain (loss) on disposition of operations on the Consolidated Statements of Operations and Comprehensive Income included amortization of ALIC's deferred gain, after-tax, of \$5 million, \$5 million and \$1 million for the years ended December 31, 2008, 2007 and 2006, respectively. DAC and DSI were reduced by \$726 million and \$70 million, respectively, as of the effective date of the transaction for balances related to the variable annuity business subject to the Reinsurance Agreements.

The separate account balances related to the modified coinsurance reinsurance were \$7.53 billion and \$13.76 billion as of December 31, 2008 and 2007, respectively. Separate account balances totaling approximately \$711 million and \$1.17 billion at December 31, 2008 and 2007, respectively, related primarily to the variable life business that is being retained by the Company, and the variable annuity business in three affiliated companies that were not included in the Agreement. In the five-months of 2006, prior to this disposition, the Company's variable annuity business generated approximately \$127 million in contract charges.

4. SUPPLEMENTAL CASH FLOW INFORMATION

Non-cash investment exchanges and modifications, which primarily reflect refinancings of fixed income securities and mergers completed with equity securities and limited partnerships, totaled \$17 million, \$72 million and \$39 million for the years ended December 31, 2008, 2007 and 2006, respectively.

Liabilities for collateral received in conjunction with the Company's securities lending and other business activities and for funds received from the Company's security repurchase business activities were \$320 million, \$1.75 billion and \$1.94 billion at December 31, 2008, 2007 and 2006, respectively, and are reported in other liabilities and accrued expenses in the Consolidated Statements of Financial Position. Obligations to return cash collateral for OTC derivatives were \$20 million, \$72 million and \$357 million at December 31, 2008, 2007 and 2006, respectively, and are reported in other liabilities and accrued expenses or other investments. Consistent with our adoption of FSP FIN 39-1 in 2008, the \$20 million of obligations to return cash collateral as of December 31, 2008 are netted against derivative positions and reported in other liabilities and accrued expenses.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The accompanying cash flows are included in cash flows from operating activities in the Consolidated Statements of Cash Flows along with the activities resulting from management of the proceeds, which for the years ended December 31 are as follows:

(\$ IN MILLIONS)	2008	2007
2006 -----		

----- NET		
CHANGE IN		
PROCEEDS		
MANAGED		
Net change		
in fixed		
income		
securities	\$ 348	\$ 34
	\$ 96	
Net change in		
short-term		
investments	1,129	443
	(159)	

Operating		
cash flow		
provided		
(used) \$	1,477	\$
	477	(63)
=====		
=====		
=====		
NET CHANGE		
IN		
LIABILITIES		
Liabilities		
for		
collateral		
and		
security		
repurchase,		
beginning		
of year \$	(1,817)	\$
	(2,294)	\$
	(2,231)	
Liabilities		
for		
collateral		
and		
security		
repurchase,		
end of		
year (340)	(1,817)	
	(2,294)	--

Operating		
cash flow		
(used)		
provided \$	(1,477)	\$
	(477)	\$ 63
=====		
=====		
=====		

In 2008, the Company recorded non-cash capital contributions totaling \$742

million, including the transfer from AIC of non-cash assets totaling \$342 million and the forgiveness by AIC of an outstanding surplus note with an unpaid principal sum of \$400 million (see Note 5).

5. RELATED PARTY TRANSACTIONS

BUSINESS OPERATIONS

The Company uses services performed by its affiliates, AIC and Allstate Investments LLC, and business facilities owned or leased and operated by AIC in conducting its business activities. In addition, the Company shares the services of employees with AIC. The Company reimburses its affiliates for the operating expenses incurred on behalf of the Company. The Company is charged for the cost of these operating expenses based on the level of services provided. Operating expenses, including compensation, retirement and other benefit programs, allocated to the Company (see Note 15), were \$467 million, \$477 million and \$494 million in 2008, 2007 and 2006, respectively. A portion of these expenses relate to the acquisition of business, which are deferred and amortized into income as described in Note 2.

STRUCTURED SETTLEMENT ANNUITIES

The Company issued \$73 million, \$74 million and \$72 million of structured settlement annuities, a type of immediate annuity, in 2008, 2007 and 2006, respectively, at prices determined using interest rates in effect at the time of purchase, to fund structured settlements in matters involving AIC. Of these amounts, \$12 million, \$11 million and \$10 million relate to structured settlement annuities with life contingencies and are included in premium income for 2008, 2007 and 2006, respectively.

In most cases, these annuities were issued under a "qualified assignment" whereby prior to July 1, 2001 Allstate Settlement Corporation ("ASC"), and on and subsequent to July 1, 2001 Allstate Assignment Corporation ("AAC"), both wholly owned subsidiaries of ALIC, purchased annuities from ALIC and assumed AIC's obligation to make future payments.

AIC issued surety bonds to guarantee the payment of structured settlement benefits assumed by ASC (from both AIC and non-related parties) and funded by certain annuity contracts issued by the Company through June 30, 2001. ASC entered into a General Indemnity Agreement pursuant to which it indemnified AIC for any liabilities associated with the surety bonds and gave AIC certain collateral security rights with respect to the annuities and certain other rights in the event of any defaults covered by the surety bonds. For contracts written on or after July 1, 2001, AIC no longer issues surety bonds to guarantee the payment of structured settlement benefits.

Alternatively, ALIC guarantees the payment of structured settlement benefits on all contracts issued on or after July 1, 2001. Reserves recorded by the Company for annuities that are guaranteed by the surety bonds of AIC were \$4.85 billion and \$4.89 billion at December 31, 2008 and 2007, respectively.

BROKER-DEALER AGREEMENT

The Company receives distribution services from Allstate Financial Services, LLC ("AFS"), an affiliated broker-dealer company, for certain variable annuity and variable life insurance contracts sold by Allstate exclusive

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agencies. For these services, the Company incurred \$19 million, \$27 million and \$44 million of commission and other distribution expenses for the years ending December 31, 2008, 2007 and 2006, respectively.

REINSURANCE TRANSACTIONS

Effective January 1, 2008, the Company's coinsurance reinsurance agreement with its unconsolidated affiliate American Heritage Life Insurance Company ("AHL"), which went into effect in 2004, was amended to include the assumption by the Company of certain accident and health insurance policies. In accordance with this amendment, the Company recorded cash of \$16 million, premium installment receivables of \$5 million, DAC of \$32 million, reserve for life-contingent contract benefits of \$24 million and accrued liabilities of \$2 million. Since the Company received assets in excess of net liabilities from an affiliate under common control, the Company recognized a gain of \$27 million (\$18 million after-tax), which was recorded as an increase to additional capital paid-in on the Company's Consolidated Statements of Financial Position.

ALIC enters into certain intercompany reinsurance transactions with its

wholly owned subsidiaries. ALIC enters into these transactions in order to maintain underwriting control and spread risk among various legal entities. These reinsurance agreements have been approved by the appropriate regulatory authorities. All significant intercompany transactions have been eliminated in consolidation.

INCOME TAXES

The Company is a party to a federal income tax allocation agreement with the Corporation (see Note 12).

SURPLUS NOTES DUE TO RELATED PARTIES

Surplus notes due to related parties outstanding at December 31 consisted of the following:

(\$ IN	
MILLIONS)	
2008	2007
-	-
-----	-----
- 5.06%	
Surplus	
Notes (1),	
due 2035	\$ 100
100	\$ 100
6.18%	
Surplus	
Notes (1),	
due 2036	100
100	100
5.93%	
Surplus	
Notes (1),	
due 2038	50
-- 7.00%	
Surplus	
Notes (1),	
due 2028	400
400	--
-----	-----

Surplus	
notes due	
to related	
parties	\$
650	\$ 200
=====	
=====	

(1) No payment of principle or interest is permitted on the surplus notes without the written approval from the proper regulatory authority (see Note 5). The regulatory authority could prohibit the payment of interest and principle on the surplus notes if certain statutory capital requirements are not met. Permission to pay interest on the surplus notes was granted in both 2008 and 2007 on all notes except the \$400 million note for which approval has not been sought.

On August 1, 2005, ALIC entered into an agreement with Kennett Capital Inc. ("Kennett"), an unconsolidated affiliate of ALIC, whereby ALIC sold to Kennett a \$100 million 5.06% surplus note due July 1, 2035 issued by ALIC Reinsurance Company ("ALIC Re"), a wholly owned subsidiary of ALIC. As payment, Kennett issued a full recourse 4.86% note due July 1, 2035 to ALIC for the same amount. As security for the performance of Kennett's obligations under the agreement and note, Kennett granted ALIC a pledge of and security interest in Kennett's right, title and interest in the surplus notes and their proceeds. Under the terms of the agreement, ALIC may sell and Kennett may choose to buy additional surplus notes, if and when additional surplus notes are issued. The note due from Kennett is classified as other investments and the related surplus notes are classified as surplus notes due to related parties in the Consolidated Statements of Financial Position. In 2008, 2007 and 2006, the Company incurred \$5 million each year of interest expense related to this surplus note, which is reflected as a component of operating costs and expenses in the Consolidated Statements of Operations and Comprehensive Income. Additionally, in 2008, 2007 and 2006, the Company recorded net investment income on the note due from Kennett of \$5 million in each year.

On June 30, 2006, under the existing agreement with Kennett discussed

above, ALIC sold Kennett a \$100 million redeemable surplus note issued by ALIC Re. The surplus note is due June 1, 2036 with an initial rate of 6.18% that will reset every ten years to the then current ten year Constant Maturity Treasury yield ("CMT"), plus 1.14%. As payment, Kennett issued a full recourse note due June 1, 2036 to ALIC for the same amount with an initial interest rate of 5.98% that will reset every ten years to the then current ten year CMT, plus 0.94%. The note due from Kennett is classified as other investments and the related surplus note is classified as surplus notes due to

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related parties in the Consolidated Statements of Financial Position. In 2008, 2007 and 2006, the Company incurred \$6 million, \$6 million and \$4 million, respectively, of interest expense related to this surplus note, which is reflected as a component of operating costs and expenses in the Consolidated Statements of Operations and Comprehensive Income. Additionally, in 2008, 2007 and 2006, the Company recorded net investment income on the note due from Kennett of \$6 million, \$6 million and \$3 million, respectively.

On June 30, 2008, under the existing agreement with Kennett, ALIC sold Kennett a \$50 million redeemable surplus note issued by ALIC Re. The surplus note is due June 1, 2038 with an initial rate of 5.93% that will reset every ten years to the then current ten year CMT, plus 2.09%. As payment, Kennett issued on June 30, 2008 a full recourse note due June 1, 2038 to ALIC for the same amount with an initial interest rate of 5.73% that will reset every ten years to the then current ten year CMT, plus 1.89%. The note due from Kennett is classified as other investments and the related surplus note is classified as surplus notes due to related parties in the Consolidated Statements of Financial Position. In 2008, the Company incurred interest expense on this surplus note of \$2 million, which is included as a component of operating costs and expenses in the Consolidated Statements of Operations and Comprehensive Income. Additionally, in 2008, the Company recorded net investment income on the note due from Kennett of \$1 million.

On August 29, 2008, the Company issued a surplus note to AIC with a principal sum of \$400 million in exchange for cash. On December 29, 2008, AIC agreed to cancel and forgive the principal and any related interest obligations associated with this surplus note. The forgiveness of the principal was recognized as a capital contribution resulting in an increase to additional capital paid-in of \$400 million.

On November 17, 2008, the Company issued a surplus note to AIC with a principal sum of \$400 million in exchange for cash. This surplus note accrues interest at a rate of 7.00% annually, which is due on the first day of April and October in each year beginning 2009 until maturity on November 17, 2028. The payment of interest and principal is subject to prior written approval from the Director of Insurance of the State of Illinois and can only be paid out of the Company's statutory-basis surplus that is in excess of certain amounts specified in the surplus note. This surplus note is included as a component of surplus notes due to related parties in the Consolidated Statements of Financial Position. In 2008, the Company incurred interest expense on this surplus note of \$3 million, which is included as a component of operating costs and expenses in the Consolidated Statements of Operations and Comprehensive Income.

NOTE PAYABLE TO PARENT

On December 27, 2006, the Company issued an intercompany note in the amount of \$500 million payable to its parent, AIC, on demand and, in any event, by March 30, 2007. This note was fully repaid in the first quarter of 2007. This note had an interest rate of 5.25%. Interest expense on this note, which totaled \$5 million in 2007, is included as a component of operating costs and expenses in the Consolidated Statements of Operations and Comprehensive Income.

REDEEMABLE PREFERRED STOCK

As of December 31, 2006, the Company's Consolidated Statements of Financial Position included redeemable preferred stock - Series A ("redeemable preferred stock") issued to Northbook Holdings, LLC, a wholly owned subsidiary of AIC. The Company's Board of Directors declared and paid cash dividends on the redeemable preferred stock from time to time, but not more frequently than quarterly. The dividends were based on the three-month LIBOR rate. Dividends of \$1 million were incurred and paid during 2006, and included as a component of operating costs and expenses on the Consolidated Statements of Operations and Comprehensive Income. During 2006, \$26 million of mandatorily redeemable preferred stock was redeemed. All remaining redeemable preferred stock was redeemed in 2007.

LIQUIDITY AND INTERCOMPANY LOAN AGREEMENT

Effective May 8, 2008, the Company, AIC and the Corporation entered into a one-year Amended and Restated Intercompany Liquidity Agreement ("Liquidity Agreement") replacing the Intercompany Liquidity Agreement between the Company and AIC, dated January 1, 2008. The Liquidity Agreement allows for short-term advances of funds to be made between parties for liquidity and other general corporate purposes. It shall be automatically renewed for subsequent one-year terms unless terminated by the parties. The Liquidity Agreement does not establish a commitment to advance funds on the part of either party. The Company and AIC each serve as a lender and borrower and the Corporation serves only as a lender. The maximum amount of advances each party may make

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or receive is limited to \$1 billion. Netting or offsetting of advances made and received is not permitted. Advances between the parties are required to have specified due dates less than or equal to 364 days from the date of the advance and be payable upon demand by written request from the lender at least ten business days prior to the demand date. The borrower may make prepayments of the outstanding principal balance of an advance without penalty. Advances will bear interest equal to or greater than the rate applicable to 30-day commercial paper issued by the Corporation on the date the advance is made with an adjustment on the first day of each month thereafter.

In addition to the Liquidity Agreement, the Company has an intercompany loan agreement with the Corporation. The amount of intercompany loans available to the Company is at the discretion of the Corporation. The maximum amount of loans the Corporation will have outstanding to all its eligible subsidiaries at any given point in time is limited to \$1.00 billion. The Company had no amounts outstanding under the intercompany loan agreement at December 31, 2008 and 2007. The Corporation may use commercial paper borrowings, bank lines of credit and repurchase agreements to fund intercompany borrowings.

INVESTMENT PURCHASES

In September 2008, in accordance with two sale agreements with AIC, the Company purchased investments from AIC. The Company paid \$944 million in cash for the investments, which included mortgage loans and privately placed corporate fixed income securities with a fair value on the date of sale of \$613 million and \$325 million, respectively, and \$6 million of accrued investment income. Since the transaction was between affiliates under common control, the mortgage loans were recorded at the outstanding principal balance, net of unamortized premium or discount, on the date of sale of \$634 million and the privately placed corporate fixed income securities were recorded at the amortized cost basis on the date of sale of \$338 million. The difference between the fair value and the outstanding principal balance, net of unamortized premium or discount, for the mortgage loans, and the amortized cost basis for the privately placed corporate fixed income securities, on the date of sale, was recorded as an increase to retained income of \$22 million after-tax (\$34 million pre-tax).

CAPITAL CONTRIBUTIONS

In June 2008, the Company received a capital contribution from AIC of \$349 million, which was recorded as additional capital paid-in on the Consolidated Statements of Financial Position. The capital contribution included fixed income securities of \$337 million, accrued investment income of \$5 million and cash of \$7 million.

In November 2008, the Company received a capital contribution from AIC of \$600 million, which was paid in cash and recorded as additional capital paid-in on the Consolidated Statements of Financial Position.

In December 2008, a surplus note issued to AIC in August 2008 was cancelled and forgiven by AIC. The forgiveness of the principal was recognized as a capital contribution resulting in an increase to additional capital paid-in of \$400 million.

The Company and AIC have a Capital Support Agreement that went into effect in 2007. Under the terms of this agreement, AIC agrees to provide capital to maintain the amount of statutory capital and surplus necessary to maintain a company action level risk-based capital ("RBC") ratio of at least 150%. AIC's obligation to provide capital to the Company under the agreement is limited to an aggregate amount of \$1 billion. Discretionary capital contributions made by AIC outside of the terms of this agreement, including the \$349 million contribution made in June 2008, the \$600 million contribution made in November 2008 and the forgiveness of the \$400 million surplus note in December 2008, do not reduce AIC's \$1 billion obligation. In exchange for providing this capital, the Company will pay AIC an annual commitment fee of 1% of the amount of the

 - - - - -
 --- Total
 fixed
 income
 securities
 \$ 49,136 \$
 1,921 \$
 (8,611) \$
 42,446
 =====
 =====
 =====

AT DECEMBER
 31, 2007
 U.S.
 government
 and
 agencies \$
 2,848 \$ 880
 \$ -- \$
 3,728
 Municipal
 4,235 115
 (39) 4,311
 Corporate
 31,624 757
 (646)
 31,735
 Foreign
 government
 1,814 374
 (3) 2,185
 Mortgage-
 backed
 securities
 3,499 37
 (46) 3,490
 Commercial
 mortgage-
 backed
 securities
 7,698 76
 (386) 7,388
 Asset-
 backed
 securities
 6,273 20
 (690) 5,603
 Redeemable
 preferred
 stock 29 1
 (1) 29 ----

 - - - - -
 --- Total
 fixed
 income
 securities
 \$ 58,020 \$
 2,260 \$
 (1,811) \$
 58,469
 =====
 =====
 =====

SCHEDULED MATURITIES

The scheduled maturities for fixed income securities are as follows at
 December 31, 2008:

AMORTIZED
 FAIR (\$ IN
 MILLIONS)
 COST VALUE

income securities
 \$ 3,112 \$
 3,589 \$
 3,505
 Mortgage loans 580
 552 508
 Equity securities
 7 4 2
 Limited partnership interests
 29 87 42
 Other investments
 121 243 257

 - - - - -
 - - - - -

Investment income, before expense
 3,849 4,475
 4,314
 Investment expense
 (129) (270)
 (257) -----

Net investment income \$
 3,720 \$
 4,205 \$
 4,057
 =====
 =====
 =====

REALIZED CAPITAL GAINS AND LOSSES, AFTER-TAX

Realized capital gains and losses by security type for the years ended December 31 are as follows:

(\$ IN MILLIONS)
 2008 2007
 2006 -----

 Fixed income securities
 \$ (2,004) \$
 (172) \$
 (157)
 Equity securities
 (29) 6 2
 Limited partnership interests
 (76) 34 2
 Derivatives
 (815) (57)
 31 Other
 (128) (8)
 43 -----

 Realized capital

gains and losses, pre-tax (3,052) (197) (79) Income tax benefit 1,067 69 28

Realized capital gains and losses, after-tax \$ (1,985) \$ (128) \$ (51)

=====
=====
=====

Realized capital gains and losses by transaction type for the years ended December 31 are as follows:

(\$ IN MILLIONS)
2008 2007 2006 -----

Sales (1) \$ 184 \$ 70 \$ (29)
Impairment write-downs (2) (1,227) (118) (21)
Change in intent write-downs (1) (3) (1,207) (92) (60)
Valuation of derivative instruments (985) (63)
(17) EMA LP income (4) (14) -- --
Settlement of derivative instruments 197 6 48 --

Realized capital gains and losses, pre-tax (3,052) (197) (79) Income tax benefit 1,067 69 28

Realized capital

gains and
 losses,
 after-tax \$
 (1,985) \$
 (128) \$
 (51)
 =====
 =====
 =====

- - - - -
- (1) To conform to the current year presentation, certain amounts in the prior years have been reclassified.
 - (2) Impairment write-downs reflect issue specific other-than-temporary declines in fair value, including instances where we could not reasonably assert that the recovery period would be temporary.
 - (3) Change in intent write-downs reflects instances where we cannot assert a positive intent to hold until recovery.
 - (4) Subsequent to October 1, 2008, income from investments in limited partnership interests accounted for utilizing the equity method of accounting is reported in realized capital gains and losses.

Gross gains of \$579 million, \$131 million and \$102 million and gross losses of \$380 million, \$186 million and \$231 million were realized on sales of fixed income securities during 2008, 2007 and 2006, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

UNREALIZED NET CAPITAL GAINS AND LOSSES

Unrealized net capital gains and losses included in accumulated other comprehensive income are as follows:

GROSS UNREALIZED FAIR ----- -----	
UNREALIZED NET (\$ IN MILLIONS) VALUE GAINS LOSSES GAINS (LOSSES) ----- ----- -----	
----- AT DECEMBER 31, 2008	
Fixed income securities \$	
42,446 \$ 1,921 \$	
(8,611) \$ (6,690)	
Equity securities	
82 1 (25) (24)	
Short-term investments 3,858	
4 (1) 3	
Derivative instruments (1)	
16 23 (9) 14 ----	
----- Unrealized net capital gains and losses, pre-tax (6,697) Amounts recognized for:	
Insurance reserves (2)	
(378) DAC and DSI	
(3) 3,493 ----- -----	
Amounts recognized 3,115	
Deferred income taxes 1,245 ----- -----	
Unrealized net	

capital gains and
 losses, after-tax
 \$ (2,337)
 =====

-
- (1) Included in the fair value of derivative securities are \$4 million classified as assets and \$(12) million classified as liabilities.
 - (2) The insurance reserves adjustment represents the amount by which the reserve balance would increase if the net unrealized gains in the applicable product portfolios were realized and reinvested at current lower interest rates, resulting in a premium deficiency. Although we evaluate premium deficiencies on the combined performance of our life insurance and immediate annuities with life contingencies, the adjustment primarily relates to structured settlement annuities with life contingencies, in addition to annuity buy-outs and certain payout annuities with life contingencies.
 - (3) The DAC and DSI adjustment represents the amount by which the amortization of DAC and DSI would increase or decrease if the unrealized gains or losses in the respective product portfolios were realized.

GROSS UNREALIZED
 FAIR -----

 UNREALIZED NET (\$
 IN MILLIONS)
 VALUE GAINS
 LOSSES GAINS
 (LOSSES) -----

 ----- AT
 DECEMBER 31, 2007
 Fixed income
 securities \$
 58,469 \$ 2,260 \$
 (1,811) \$ 449
 Equity securities
 102 5 (5) --
 Derivative
 instruments (1)
 (32) -- (32) (32)

 - Unrealized net
 capital gains and
 losses, pre-tax
 417 Amounts
 recognized for:
 Insurance
 reserves (1,059)
 DAC and DSI 513 -

 Amounts
 recognized (546)
 Deferred income
 taxes 45 -----

 Unrealized net
 capital gains and
 losses, after-tax
 \$ (84)
 =====

-
- (1) Included in the fair value of derivative securities are \$(9) million classified as assets and \$23 million classified as liabilities.

CHANGE IN UNREALIZED NET CAPITAL GAINS AND LOSSES

The change in unrealized net capital gains and losses for the years ended December 31 is as follows:

(\$ IN
 MILLIONS)
 2008 2007
 2006 -----

```

-----
-----
Fixed
income
securities
$ (7,139)
$ (1,139)
$ (672)
Equity
securities
(24) (11)
6 Short-
term
investments
3 -- --
Derivative
instruments
46 (16)
(10) -----
-----
-----
Total
(7,114)
(1,166)
(676)
Amounts
recognized
for:
Insurance
reserves
681 70 214
DAC and
DSI 2,980
467 58 ---
-----
-----
- Increase
in amounts
recognized
3,661 537
272
Deferred
income
taxes
1,200 220
141 -----
-----
-----
Change in
unrealized
net
capital
gains and
losses $
(2,253) $
(409) $
(263)
=====
=====
=====

```

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

PORTFOLIO MONITORING

Inherent in the Company's evaluation of a particular security are assumptions and estimates about the financial condition of the issue or issuer and its future earnings potential. Some of the factors considered in evaluating whether a decline in fair value is other than temporary are: 1) the Company's ability and intent to retain the investment for a period of time sufficient to allow for an anticipated recovery in value; 2) the expected recoverability of principal and interest; 3) the length of time and extent to which the fair value has been less than amortized cost for fixed income securities, or cost for equity securities; 4) the financial condition, near-term and long-term prospects

of the issue or issuer, including relevant industry conditions and trends, and implications of rating agency actions and offering prices; and 5) the specific reasons that a security is in a significant unrealized loss position, including market conditions which could affect access to liquidity.

The following table summarizes the gross unrealized losses and fair value of fixed income and equity securities by the length of time that individual securities have been in a continuous unrealized loss position.

(\$ IN
MILLIONS)
LESS THAN
12 MONTHS
12 MONTHS
OR MORE --

TOTAL
NUMBER
FAIR
UNREALIZED
NUMBER
FAIR
UNREALIZED
UNREALIZED
OF ISSUES
VALUE
LOSSES OF
ISSUES
VALUE
LOSSES
LOSSES ---

--- AT
DECEMBER
31, 2008
Fixed
income
securities
Municipal
400 \$
2,460 \$
(653) 26 \$
199 \$ (43)
\$ (696)
Corporate
1,282
12,781
(1,779)
446 4,344
(1,776)
(3,555)
Foreign
government
43 304
(53) 2 13
(12) (65)
MBS 129
724 (142)
57 233
(121)
(263) CMBS
289 2,646
(786) 176
901
(1,206)
(1,992)
ABS 141
778 (251)
335 1,666

are related to unrealized losses on investment grade fixed income securities. Investment grade is defined as a security having a rating from the NAIC of 1 or 2; a rating of Aaa, Aa, A or Baa from Moody's, a rating of AAA, AA, A or BBB from Standard & Poor's ("S&P"), Fitch or Dominion, or a rating of aaa, aa, a or bbb from A.M. Best; or a comparable internal rating if an externally provided rating is not available. Unrealized losses on investment grade securities are principally related to rising interest rates or changes in credit spreads since the securities were acquired.

As of December 31, 2008, the remaining \$6.93 billion of unrealized losses are related to securities in unrealized loss positions greater than or equal to 20% of cost or amortized cost. Of the \$6.93 billion, \$705 million are related to below investment grade fixed income securities and \$22 million are related to equity securities. Of these

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

amounts, \$13 million of the below investment grade fixed income securities had been in an unrealized loss position for a period of twelve or more consecutive months as of December 31, 2008. Unrealized losses on below investment grade securities are principally related to rising interest rates or changes in credit spreads. Unrealized losses on equity securities are primarily related to equity market fluctuations. The Company expects eventual recovery of these securities. Every security was included in our portfolio monitoring process.

The securities comprising the \$6.93 billion of unrealized losses were evaluated based on factors such as the financial condition and near-term and long-term prospects of the issuer and were determined to have adequate resources to fulfill contractual obligations, such as recent financings or bank loans, cash flows from operations, collateral or the position of a subsidiary with respect to its parent's bankruptcy.

Unrealized losses on mortgage-backed, asset-backed and commercial mortgage-backed holdings were evaluated based on credit ratings, as well as the performance of the underlying collateral relative to the securities' positions in the securities' respective capital structure. The unrealized losses on municipal bonds and asset-backed securities that had credit enhancements from bond insurers were evaluated on the quality of the underlying security. These investments were determined to have adequate resources to fulfill contractual obligations.

As of December 31, 2008, the Company had the intent and ability to hold the fixed income and equity securities with unrealized losses for a period of time sufficient for them to recover.

LIMITED PARTNERSHIP IMPAIRMENT

As of December 31, 2008 and 2007, equity method limited partnership interests totaled \$627 million and \$485 million, respectively. The Company recognizes a loss in value for equity method investments when evidence demonstrates that it is other-than-temporarily impaired. Evidence of a loss in value that is other than temporary may include the absence of an ability to recover the carrying amount of the investment or the inability of the investee to sustain an earnings capacity that would justify the carrying amount of the investment. In 2008 and 2007, the Company had write-downs of \$13 million and \$9 million, respectively, related to equity method limited partnership interests. No write-downs were recognized in 2006.

As of December 31, 2008 and 2007, the carrying value for cost method limited partnership interests was \$560 million and \$509 million, respectively, which primarily included limited partnership interests in fund investments. To determine if an other-than-temporary impairment has occurred, the Company evaluates whether an impairment indicator has occurred in the period that may have a significant adverse effect on the carrying value of the investment. Impairment indicators may include: actual recent cash flows received being significantly less than expected cash flows; reduced valuations based on financing completed at a lower value; completed sale of a material underlying investment at a price significantly lower than expected; or any other recent adverse events since the last financial statements received that might affect the fair value of the investee's capital. Additionally, the Company uses a screening process to identify those investments whose net asset value is below established thresholds for certain periods of time, and investments that are performing below expectations for consideration for inclusion on its watch-list. In 2008, 2007 and 2006 the Company had write-downs of \$53 million, \$0.3 million and \$0.1 million, respectively, related to cost method investments that were other-than-temporarily impaired.

MORTGAGE LOAN IMPAIRMENT

A mortgage loan is impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement.

The net carrying value of impaired loans at December 31, 2008 and 2007 was \$159 million and \$2 million, respectively. Valuation allowances of \$3 million were held at December 31, 2008 reflecting a charge to operations related to impaired mortgage loans. No valuation allowances were held at December 31, 2007 because the fair value of the collateral was greater than the recorded investment in the loans, and no valuation allowances were charged to operations during the years 2007 or 2006. Realized capital losses due to changes in intent to hold mortgage loans to maturity totaled \$73 million and \$28 million for the years ended December 31, 2008 and 2007, respectively.

Interest income for impaired loans is recognized on an accrual basis if payments are expected to continue to be received; otherwise cash basis is used. The Company recognized interest income on impaired loans of \$6 million, \$0.2 million and \$0.4 million during 2008, 2007 and 2006, respectively. The average balance of impaired loans was \$43 million, \$3 million and \$5 million in 2008, 2007 and 2006, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

INVESTMENT CONCENTRATION FOR MUNICIPAL BOND AND COMMERCIAL MORTGAGE PORTFOLIOS

The Company maintains a diversified portfolio of municipal bonds. The following table shows the principal geographic distribution of municipal bond issuers represented in the Company's portfolio. No other state represents more than 5% of the portfolio at December 31.

(% OF MUNICIPAL BOND PORTFOLIO CARRYING VALUE)	
2008	2007
-----	-----
California	
18.3 %	
19.7 %	
Delaware	
9.3	8.1
Texas	8.9
9.0	New
York	8.9
9.5	New
Jersey	7.2
7.1	
Virginia	
6.0	4.7
Oregon	5.3
5.2	

The Company's mortgage loans are collateralized by a variety of commercial real estate property types located throughout the United States. Substantially all of the commercial mortgage loans are non-recourse to the borrower. The following table shows the principal geographic distribution of commercial real estate represented in the Company's mortgage portfolio. No other state represented more than 5% of the portfolio at December 31.

(% OF COMMERCIAL MORTGAGE PORTFOLIO CARRYING VALUE)	
2008	2007
-----	-----
California	
21.0 %	22.7
% Illinois	
9.0	8.7
Texas	7.0
7.3	

Pennsylvania
 6.2 5.5 New
 Jersey 6.1
 5.5 New
 York 5.8
 5.7

The types of properties collateralizing the commercial mortgage loans at December 31 are as follows:

(% OF COMMERCIAL MORTGAGE PORTFOLIO CARRYING VALUE)	
2008	2007

Office buildings	
32.5 %	35.3 %
Retail	
24.5	23.1
Warehouse	
22.6	21.3
Apartment complex	
15.5	15.8
Other	
4.5	-----

---- Total	
100.0 %	100.0 %
=====	=====
=====	=====

The contractual maturities of the commercial mortgage loan portfolio as of December 31, 2008 for loans that were not in foreclosure are as follows:

NUMBER CARRYING (\$ IN MILLIONS) OF LOANS VALUE	PERCENT

2009 81 \$	746 7.5 %
2010 94	1,182 11.8
2011 106	1,434 14.3
2012 106	1,321 13.2
2013 82 780	7.8
Thereafter	445 4,549
45.4	-----

Total 914 \$	10,012
100.0 %	-----
=====	=====
=====	=====
=====	=====

In 2008, \$423 million of commercial mortgage loans were contractually due. Of these, 79% were paid as due, 2% were refinanced at prevailing market terms and 18% were extended generally for less than one year. 1% was in the process

of foreclosure, and none were foreclosed or in the process of refinancing or restructuring discussions.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CONCENTRATION OF CREDIT RISK

At December 31, 2008, other than U.S. government and agencies, the Company's exposure to credit concentration risk to a single issuer and its affiliates of greater than 10% of shareholder's equity includes the following:

(\$ IN MILLIONS)

PERCENTAGE OF
PERCENTAGE OF
CARRYING
STOCKHOLDER'S
TOTAL VALUE
EQUITY
INVESTMENTS ---

----- Federal
Home Loan
Mortgage
Corporation
("Freddie Mac")
Fixed income
securities \$ 61
Mortgage loans
30 Short-term
investments 199

Total Freddie
Mac \$ 290 13.1%
0.5%

=====
Bank of America
Corporation
Fixed income
securities \$
283 Equity
securities 7
Derivative
instruments (2)

Total Bank of
America
Corporation \$
288 13.0 0.5
=====

Federal
National
Mortgage
Association
("Fannie Mae")
Fixed income
securities \$
267 -----
----- Total
Fannie Mae \$
267 12.1 0.4
=====

Wells Fargo &
Company Fixed
income
securities \$
227 Derivative
instruments (1)

Total Wells
Fargo & Company
\$ 226 10.2 0.4
=====

SECURITIES LOANED

The Company's business activities include securities lending programs with third parties, mostly large banks. At December 31, 2008 and 2007, fixed income and equity securities with a carrying value of \$307 million and \$1.70 billion, respectively, were on loan under these agreements. In return, the Company receives cash that it invests and includes in short-term investments and fixed income securities, with an offsetting liability recorded in other liabilities and accrued expenses to account for the Company's obligation to return the collateral. Interest income on collateral, net of fees, was \$34 million, \$11 million and \$5 million, for the years ended December 31, 2008, 2007 and 2006, respectively.

OTHER INVESTMENT INFORMATION

Included in fixed income securities are below investment grade assets totaling \$1.73 billion and \$2.66 billion at December 31, 2008 and 2007, respectively.

At December 31, 2008, fixed income securities with a carrying value of \$66 million were on deposit with regulatory authorities as required by law.

At December 31, 2008, the carrying value of fixed income securities that were non-income producing was \$4 million. No other investments were non-income producing at December 31, 2008.

7. FINANCIAL INSTRUMENTS

In the normal course of business, the Company invests in various financial assets, incurs various financial liabilities and enters into agreements involving derivative financial instruments and other off-balance-sheet financial instruments.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table summarizes the Company's financial assets and financial liabilities measured at fair value on a recurring and non-recurring basis as of December 31, 2008:

QUOTED PRICES SIGNIFICANT IN ACTIVE OTHER SIGNIFICANT MARKETS FOR OBSERVABLE UNOBSERVABLE BALANCE AS OF IDENTICAL ASSETS INPUTS INPUTS OTHER VALUATIONS DECEMBER 31, (\$ IN MILLIONS) (LEVEL 1) (LEVEL 2) (LEVEL 3) AND NETTING 2008 --- ----- ----- ----- -----			
FINANCIAL			
ASSETS: Fixed			
income			
securities \$ 276			
\$ 28,037 \$			
14,133 \$ 42,446			
Equity			
securities 1 54			
27 82 Short-term			
investments 342			
3,516 -- 3,858			
Other			
investments:			
Free-standing			
derivatives --			
605 13 618 ----- ----- ----- -----			

TOTAL RECURRING
BASIS ASSETS 619
32,212 14,173
47,004 Non-
recurring basis
-- -- 244 244
Valued at cost,
amortized cost
or using the
equity method \$
13,004 13,004
Counterparty and
cash collateral
netting (1)
(480) (480) ----

TOTAL
INVESTMENTS 619
32,212 14,417
12,524 59,772 --

Separate account
assets 8,239 --
-- -- 8,239
Other assets (1)
-- 1 -- -- ----

TOTAL FINANCIAL
ASSETS \$ 8,857 \$
32,212 \$ 14,418
\$ 12,524 \$
68,011

=====
=====
=====
=====
=====

% of Total
financial assets
13.0% 47.4%
21.2% 18.4%

100.0% FINANCIAL
LIABILITIES:

Contractholder
funds:
Derivatives
embedded in
annuity
contracts \$ -- \$
(37) \$ (265) \$
(302) Other
liabilities:
Free-standing
derivatives --
(1,118) (106)
(1,224) Non-
recurring basis
-- -- --

Counterparty and
cash collateral
netting (1) \$
460 460 -----

TOTAL FINANCIAL
LIABILITIES \$ --

\$ (1,155) \$
 (371) \$ 460 \$
 (1,066)

=====
 =====
 =====
 =====
 =====

% of Total
 financial
 liabilities --%
 108.4% 34.8%
 (43.2)% 100.0%

(1) In accordance with FSP FIN 39-1, the Company nets all fair value amounts recognized for derivative instruments and fair value amounts recognized for the right to reclaim cash collateral or the obligation to return cash collateral executed with the same counterparty under a master netting agreement. At December 31, 2008, the right to reclaim cash collateral was offset by securities held, and the obligation to return collateral was \$20 million.

As required by SFAS No. 157, when the inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measurement in its entirety. Thus, a Level 3 fair value measurement may include inputs that are observable (Level 1 or Level 2) and unobservable (Level 3). Gains and losses for such assets and liabilities categorized within Level 3 may include changes in fair value that are attributable to both observable inputs (Level 1 and Level 2) and unobservable inputs (Level 3). Net transfers in and/or out of Level 3 are reported as having occurred at the beginning of the quarter the transfer occurred; therefore, for all transfers into Level 3, all realized and unrealized gains and losses in the quarter of transfer are reflected in the table below. Further, it should be noted that the following table does not take into consideration the effect of offsetting Level 1 and Level 2 financial instruments entered into that economically hedge certain exposures to the Level 3 positions.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table provides a summary of changes in fair value during the year ended December 31, 2008 of Level 3 financial assets and financial liabilities held at fair value on a recurring basis at December 31, 2008.

TOTAL REALIZED
 AND UNREALIZED
 GAINS (LOSSES)
 INCLUDED IN: ----

 ----- OCI ON
 STATEMENT OF
 PURCHASES, SALES,
 BALANCE AS OF NET
 FINANCIAL
 ISSUANCES AND (\$
 IN MILLIONS)
 JANUARY 1, 2008
 INCOME (1)
 POSITION
 SETTLEMENTS, NET

 FINANCIAL ASSETS
 Fixed income
 securities \$
 18,830 \$ (1,617)
 \$ (3,029) \$
 (2,322) Equity
 securities 61 (3)
 (12) 20 Other
 investments:
 Free-standing
 derivatives, net
 (6) (125) -- 38 -


```

=====
=====
=====
FINANCIAL
LIABILITIES
Contractholder
funds:
Derivatives
embedded in
annuity contracts
$ -- $ (265) $
(270) -----
-----
--- TOTAL
RECURRING LEVEL 3
FINANCIAL
LIABILITIES $ --
$ (265) $ (270)
=====
=====
=====

```

- (1) The effect to net income of financial assets and financial liabilities totals \$(2.02) billion and is reported in the Consolidated Statements of Operations and Comprehensive Income as follows: \$(1.83) billion in realized capital gains and losses; \$91 million in net investment income; \$(6) million in interest credited to contractholder funds; and \$(270) million in contract benefits.
- (2) Comprises \$13 million of financial assets and \$(106) million of financial liabilities.
- (3) Comprises \$14.17 billion of investments and \$(106) million of free-standing derivatives included in financial liabilities.
- (4) The amounts represent gains and losses included in net income for the period of time that the financial asset or financial liability was determined to be in Level 3. These gains and losses total \$(1.65) billion and are reported in the Consolidated Statements of Operations and Comprehensive Income as follows: \$(1.45) billion in realized capital gains and losses; \$75 million in net investment income; \$(1) million in interest credited to contractholder funds and \$(270) million in contract benefits.

Presented below are the fair value estimates of financial instruments including those reported at fair value and discussed above and those reported using other methods for which a description of the method to determine fair value appears below the following tables.

FINANCIAL ASSETS

```

DECEMBER
31, 2008
DECEMBER
31, 2007 --
-----
-----
-----
- CARRYING
FAIR
CARRYING
FAIR ($ IN
MILLIONS)
VALUE VALUE
VALUE VALUE
-----
-----
-----
Fixed
income
securities
(1) $
42,446 $
42,446 $
58,469 $
58,469
Equity

```

securities		
(1) 82	82	
102	102	
Mortgage		
loans		
10,012		
8,700	9,901	
9,804		
Limited		
partnership		
interests -		
cost basis		
560	541	509
525	Short-	
term		
investments		
(1) 3,858		
3,858	386	
386	Bank	
loans	981	
675	1,128	
1,085	Free-	
standing		
derivatives		
(1) 138	138	
457	457	
Intercompany		
notes	250	
185	200	186
Separate		
accounts		
(1) 8,239		
8,239		
14,929		
14,929		

(1) Carried at fair value in the Consolidated Statements of Financial Position.

The fair value of mortgage loans is based on discounted contractual cash flows. Risk adjusted discount rates are selected using current rates at which similar loans would be made to borrowers with similar characteristics, using similar types of properties as collateral. The fair value of limited partnership interests accounted for on the cost basis is determined using reported net asset values of the underlying funds. The fair value of bank loans, which are

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

reported in other investments on the Consolidated Statements of Financial Position, are valued based on broker quotes from brokers familiar with the loans. The fair value of intercompany notes is based on discounted cash flow calculations using current interest rates for instruments with comparable terms.

FINANCIAL LIABILITIES

DECEMBER 31,	
2008	DECEMBER
31, 2007	----

----	CARRYING
FAIR	CARRYING
FAIR (\$ IN	
MILLIONS)	
VALUE	VALUE
VALUE	VALUE

Contractholder	
funds on	
investment	
contracts (2)	
\$ 45,989	\$

42,484 \$
 50,445 \$
 49,117
 Surplus notes
 due to
 related
 parties 650
 566 200 189
 Liability for
 collateral
 (1) 340 340
 1,817 1,817
 Free-standing
 derivatives
 (1) 744 744
 292 292

 (1) Carried at fair value in the Consolidated Statements of Financial Position.

(2) As of December 31, 2008 and 2007, contractholder funds on investment contracts exclude contractholder funds related to interest-sensitive life insurance, variable annuities and variable life insurance totaling \$10.79 billion and \$10.02 billion, respectively.

Beginning in 2008, the fair value of contractholder funds on investment contracts is based on the terms of the underlying contracts utilizing prevailing market rates for similar contracts adjusted for credit risk. Deferred annuities included in contractholder funds are valued using discounted cash flow models which incorporate market value margins, which are based on the cost of holding economic capital, and the Company's own credit risk. Immediate annuities without life contingencies and fixed rate funding agreements are valued at the present value of future benefits using market implied interest rates which include the Company's own credit risk. In 2007, the fair value of investment contracts was based on the terms of the underlying contracts. Fixed annuities were valued at the account balance less surrender charges. Immediate annuities without life contingencies and fixed rate funding agreements were valued at the present value of future benefits using current interest rates. The fair value of variable rate funding agreements approximated the carrying value. Market value adjusted annuities' fair value was estimated to be the market adjusted surrender value. Equity-indexed annuity contracts' fair value approximated the carrying value since the embedded equity options are carried at fair value.

The fair value of surplus notes due to related parties is based on discounted cash flow calculations using current interest rates for instruments with comparable terms and considers the Company's own credit risk. The liability for collateral is valued at carrying value due to its short-term nature.

DERIVATIVE FINANCIAL INSTRUMENTS

The Company primarily uses derivatives for risk reduction and asset replication. In addition, the Company has derivatives embedded in financial instruments, which are required to be separated and accounted for as derivative instruments. With the exception of derivatives used for asset replication and embedded derivatives which are required to be separated, all of the Company's derivatives are evaluated for their ongoing effectiveness as either accounting or non-hedge derivative financial instruments on at least a quarterly basis (see Note 2). The Company does not use derivatives for trading purposes. Non-hedge accounting is used for "portfolio" level hedging strategies where the terms of the individual hedged items do not meet the strict homogeneity requirements prescribed in SFAS No. 133 to permit the application of SFAS No. 133's hedge accounting model. The principal benefit of a "portfolio" level strategy is in its cost savings through its ability to use fewer derivatives with larger notional amounts.

The Company uses derivatives to partially mitigate potential adverse impacts from future increases in credit spreads. Credit default swaps are used to mitigate the credit spread risk within the Company's fixed income portfolio.

Asset-liability management is a risk management strategy that is principally employed to align the respective interest-rate sensitivities of the Company's assets and liabilities. Depending upon the attributes of the assets acquired and liabilities issued, derivative instruments such as interest rate swaps, caps and floors are acquired to change the interest rate characteristics of existing assets and liabilities to ensure a properly matched relationship is maintained within specific ranges and to reduce exposure to rising or falling interest rates. The Company uses financial futures to hedge anticipated asset purchases and liability issuances and financial futures and options for hedging the Company's equity exposure contained in equity indexed annuity product

contracts that offer equity returns to contractholders. In addition, the Company also uses interest rate swaps to hedge interest rate risk inherent

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

in funding agreements and foreign currency swaps primarily to reduce the foreign currency risk associated with issuing foreign currency denominated funding agreements.

Asset replication refers to the "synthetic" creation of an asset through the use of a credit derivative and a high quality cash instrument to replicate fixed income securities that are either unavailable in the cash bond market or more economical to acquire in synthetic form. The Company replicates fixed income securities using a combination of a credit default swap and one or more highly rated fixed income securities to synthetically replicate the economic characteristics of one or more cash market securities.

The Company has derivatives that are embedded in non-derivative "host" contracts. The Company's primary embedded derivatives are conversion options in fixed income securities, which provide the Company with the right to convert the instrument into a predetermined number of shares of common stock; equity options in annuity product contracts, which provide equity returns to contractholders; and equity-indexed notes containing equity call options, which provide a coupon payout based upon one or more equity-based indices.

The notional amounts specified in the contracts are used to calculate the exchange of contractual payments under the agreements and are generally not representative of the potential for gain or loss on these agreements. However, the notional amounts specified in credit default swaps represent the maximum amount of potential loss, assuming no recoveries.

Fair value, which is equal to the carrying value, is the estimated amount that the Company would receive (pay) to terminate the derivative contracts at the reporting date. The fair value valuation techniques are described in Note 2. For certain exchange traded derivatives, the exchange requires margin deposits as well as daily cash settlements of margin accounts. As of December 31, 2008, the Company pledged \$28 million of securities in the form of margin deposits.

Carrying value amounts include the fair value of the derivatives, including the embedded derivatives, and exclude the accrued periodic settlements which are short term in nature and are reported in accrued investment income or other invested assets. The carrying value amounts for free-standing derivatives have been further adjusted for the effects, if any, of legally enforceable master netting agreements.

Derivative instruments are recorded at fair value and presented in the Consolidated Statements of Financial Position as of December 31, as follows:

CARRYING	
VALUE -----	

---- ASSETS	
(LIABILITIES)	

----- (\$	
IN MILLIONS)	
2008 2007	
2008 2007 ---	

- Fixed	
income	
securities \$	
222 \$ 612 \$ -	
- \$ -- Other	
investments	
138 444 -- --	
Other assets	
3 2 -- --	
Contractholder	
funds -- --	
(302) (119)	
Other	

liabilities
 and accrued
 expenses -- -
 - (744) (292)

 ----- Total \$
 363 \$ 1,058 \$
 (1,046) \$
 (411)
 =====
 =====
 =====
 =====

For cash flow hedges, unrealized net pre-tax losses included in accumulated other comprehensive income were \$16 million and \$(32) million at December 31, 2008 and 2007, respectively. The net pre-tax changes in accumulated other comprehensive income due to cash flow hedges were \$48 million, \$(16) million and \$(10) million in 2008, 2007 and 2006, respectively. Amortization of net gains from accumulated other comprehensive income related to cash flow hedges is expected to be \$(1) million in 2009.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table summarizes the notional amount, fair value and carrying value of the Company's derivative financial instruments at December 31, 2008.

CARRYING
 VALUE
 NOTIONAL FAIR

 ----- (\$ IN
 MILLIONS)
 AMOUNT VALUE
 ASSETS
 (LIABILITIES)

 INTEREST RATE
 CONTRACTS
 Interest rate
 swap
 agreements \$
 10,354 \$
 (799) \$ 22 \$
 (821)
 Financial
 futures
 contracts and
 options 4,359
 (1) -- (1)
 Interest rate
 cap and floor
 agreements
 5,688 (35) 2
 (37) -----

 Total
 interest rate
 contracts
 20,401 (835)
 24 (859)
 EQUITY AND
 INDEX
 CONTRACTS
 Options,
 financial
 futures, and

 Total
 interest
 rate
 contracts
 29,356 (290)
 (110) (180)
 EQUITY AND
 INDEX
 CONTRACTS
 Options,
 financial
 futures, and
 warrants
 6,057 106
 176 (70)
 FOREIGN
 CURRENCY
 CONTRACTS
 Foreign
 currency
 swap
 agreements
 1,493 361
 388 (27)
 CREDIT
 DEFAULT
 SWAPS USED
 FOR ASSET
 REPLICATION
 Credit
 default
 swaps -
 selling
 protection
 631 (23)
 (10) (13)
 EMBEDDED
 DERIVATIVE
 FINANCIAL
 INSTRUMENTS
 Guaranteed
 accumulation
 benefits
 1,592 -- --
 --
 Guaranteed
 withdrawal
 benefits
 1,216 -- --
 --
 Conversion
 options in
 fixed income
 securities
 559 190 190
 -- Equity-
 indexed call
 options in
 fixed income
 securities
 800 422 422
 -- Equity-
 indexed and
 forward
 starting
 options in
 life and
 annuity
 product
 contracts
 3,934 (123)
 -- (123)
 Other
 embedded
 derivative
 financial
 instruments


```

-----
--
-----
-----
Subtotal -
- 120 65
60 -- 245
(48) -----
-----
-----
-----
-----
TOTAL
$ 10 $ 145
$ 180 $
171 $ 11 $
517 $ (73)
=====
=====
=====
=====
=====
=====
=====
=====
=====
=====

```

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

In selling protection with CDS, the Company sells credit protection on an identified single name, a basket of names in a first-to-default ("FTD") structure or credit derivative index ("CDX") that is generally investment grade, and in return receives periodic premiums through expiration or termination of the agreement. With single name CDS, this premium or credit spread generally corresponds to the difference between the yield on the referenced entity's public fixed maturity cash instruments and swap rates, at the time the agreement is executed. With FTD baskets, because of the additional credit risk inherent in a basket of named credits, the premium generally corresponds to a high proportion of the sum of the credit spreads of the names in the basket and the correlation between the names. CDX index is utilized to take a position on multiple (generally 125) reference entities. Credit events are typically defined as bankruptcy, failure to pay, or restructuring, depending on the nature of the reference credit. If a credit event occurs, the Company settles with the counterparty, either through physical settlement or cash settlement. In a physical settlement, a reference asset is delivered by the buyer of protection to the Company, in exchange for cash payment at par, while in a cash settlement, the Company pays the difference between par and the prescribed value of the reference asset. When a credit event occurs in a single name or FTD basket (for FTD, the first credit event occurring for any one name in the basket), the contract terminates at time of settlement. For CDX index, the reference entity's name incurring the credit event is removed from the index while the contract continues until expiration. The maximum payout on a CDS is the contract notional amount. A physical settlement may afford the Company with recovery rights as the new owner of the asset.

The Company monitors risk associated with credit derivatives through individual name credit limits at both a credit derivative and a combined cash instrument/credit derivative level. The ratings of individual names for which protection has been sold are also monitored.

OFF-BALANCE-SHEET FINANCIAL INSTRUMENTS AND UNCONSOLIDATED INVESTMENTS IN VIES

The contractual amounts and fair values of off-balance-sheet financial instruments at December 31 are as follows:

```

2008 2007
-----
-----
-----
-----
-----
-----
-----
CONTRACTUAL
FAIR
CONTRACTUAL
FAIR ($ IN
MILLIONS)
AMOUNT
VALUE

```

AMOUNT
VALUE ----

Commitments to invest in limited partnership interests
\$ 1,075
-- \$ 1,198
\$ --
Commitments to invest - other 2
-- 12 --
Commitments to extend mortgage loans 3 --
326 3
Private placement commitments
-- -- 30 -
-

In the preceding table, the contractual amounts represent the amount at risk if the contract is fully drawn upon, the counterparty defaults and the value of any underlying security becomes worthless. Unless noted otherwise, the Company does not require collateral or other security to support off-balance-sheet financial instruments with credit risk.

Commitments to invest generally represent commitments to acquire financial interests or instruments. The Company enters into these agreements to allow for additional participation in certain limited partnership investments. Because the equity investments in the limited partnerships are not actively traded, it is not practical to estimate the fair value of these commitments.

Commitments to extend mortgage loans are agreements to lend to a borrower provided there is no violation of any condition established in the contract. The Company enters into these agreements to commit to future loan fundings at a predetermined interest rate. Commitments generally have fixed expiration dates or other termination clauses. Commitments to extend mortgage loans, which are secured by the underlying properties, are valued based on estimates of fees charged by other institutions to make similar commitments to similar borrowers.

Private placement commitments represent conditional commitments to purchase private placement debt and equity securities at a specified future date. The Company regularly enters into these agreements in the normal course of business. The fair value of these commitments generally cannot be estimated on the date the commitment is made as the terms and conditions of the underlying private placement securities are not yet final.

In 2006, the Company participated in the establishment of an investment management variable interest entity ("VIE") that holds assets under the management of Allstate Investment Management Company, an unconsolidated affiliate of the Company, on behalf of unrelated third party investors. The VIE had assets primarily consisting of

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

investment securities and cash totaling \$400 million and liabilities primarily consisting of long-term debt totaling \$378 million at December 31, 2008. The Company does not consolidate the VIE because it is not the primary beneficiary. The Company's maximum loss exposure related to the VIE is the amortized cost of its investment, which was \$7 million at December 31, 2008.

8. RESERVE FOR LIFE-CONTINGENT CONTRACT BENEFITS AND CONTRACTHOLDER FUNDS

At December 31, the reserve for life-contingent contract benefits consists of the following:

(\$ IN

11.7% future
benefits
expectancy
Other
immediate
fixed
annuities
1983 group
annuity
mortality
table; 1983
Interest
rate Present
value of
expected
individual
annuity
mortality
table;
Annuity
assumptions
range future
benefits
based on
2000
mortality
table with
internal
modifications
from 1.6% to
11.5%
historical
experience
Traditional
life
insurance
Actual
company
experience
plus loading
Interest
rate Net
level
premium
reserve
assumptions
range method
using the
Company's
from 4.0% to
11.3%
withdrawal
experience
rates Other:
Variable
annuity
guaranteed
100% of
Annuity 2000
mortality
table
Interest
rate
Projected
benefit
ratio
minimum
death
benefits (1)
assumptions
range
applied to
cumulative
from 5.3% to
5.9%
assessments
Accident and
health
Actual
company
experience

credited range
 Either a percentage
 of account balance
 or from 2.0% to 6.0%
 dollar amount
 grading off
 generally over 20
 years Fixed
 annuities Interest
 rates credited range
 Either a declining
 or a level
 percentage charge
 from 1.3% to 11.5%
 for immediate
 generally over nine
 years or less.
 annuities and 0% to
 16.0% for
 Additionally,
 approximately 28.4%
 of fixed other fixed
 annuities (which
 annuities are
 subject to market
 value include
 equity-indexed
 annuities adjustment
 for discretionary
 withdrawals whose
 returns are indexed
 to the S&P 500)
 Funding agreements
 backing Interest
 rates credited range
 Not applicable
 medium-term notes
 from 0.5% to 6.5%
 (excluding currency-
 swapped medium-term
 notes) Other
 investment
 contracts: Variable
 guaranteed minimum
 Interest rates used
 in Withdrawal and
 surrender charges
 are based on income,
 accumulation and
 establishing
 reserves range from
 the terms of the
 related interest-
 sensitive withdrawal
 benefits (1) and
 1.8% to 10.3% life
 insurance or fixed
 annuity contract
 secondary guarantees
 on interest-
 sensitive life
 insurance and fixed
 annuities

- - - - -
 (1) In 2006, the Company disposed of substantially all of its variable annuity
 business through reinsurance agreements with Prudential (see Note 3).

Contractholder funds include funding agreements held by VIEs issuing
 medium-term notes. The VIEs are Allstate Life Funding, LLC, Allstate Financial
 Global Funding, LLC, Allstate Life Global Funding and Allstate Life Global
 Funding II, and their primary assets are funding agreements used exclusively to
 back medium-term note programs.

Contractholder funds activity for the years ended December 31 is as
 follows:

(\$ IN
 MILLIONS)
 2008 2007 --

```

-----
Balance,
beginning of
year $
60,464 $
60,565
Deposits
9,286 7,960
Interest
credited
2,350 2,635
Benefits
(1,701)
(1,656)
Surrenders
and partial
withdrawals
(4,329)
(4,928)
Maturities
of
institutional
products
(8,599)
(3,165) Net
transfers
from
separate
accounts 19
13 Contract
charges
(819) (751)
Fair value
hedge
adjustments
for
institutional
products
(56) 34
Other
adjustments
165 (243) --
-----
Balance, end
of year $
56,780 $
60,464
=====
=====

```

The Company offered various guarantees to variable annuity contractholders. Liabilities for variable contract guarantees related to death benefits are included in the reserve for life-contingent contract benefits and the liabilities related to the income, withdrawal and accumulation benefits are included in contractholder funds in the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Statements of Financial Position. All liabilities for variable contract guarantees are reported on a gross basis on the balance sheet with a corresponding reinsurance recoverable asset for those contracts subject to reinsurance, including the Prudential Reinsurance Agreements as disclosed in Note 3.

Absent any contract provision wherein the Company guarantees either a minimum return or account value upon death, a specified contract anniversary date, partial withdrawal or annuitization, variable annuity and variable life insurance contractholders bear the investment risk that the separate accounts' funds may not meet their stated investment objectives. The account balances of variable annuities contracts' separate accounts with guarantees included \$7.07 billion and \$13.32 billion of equity, fixed income and balanced mutual funds and \$730 million and \$661 million of money market mutual funds at December 31, 2008 and 2007, respectively.

The table below presents information regarding the Company's variable

annuity contracts with guarantees. The Company's variable annuity contracts may offer more than one type of guarantee in each contract; therefore, the sum of amounts listed exceeds the total account balances of variable annuity contracts' separate accounts with guarantees.

(\$ IN MILLIONS)

DECEMBER 31, --

----- 2008

2007 -----

IN THE EVENT OF

DEATH Separate

account value \$

7,802 \$ 13,939

Net amount at

risk (1) \$

3,971 \$ 956

Average

attained age of

contractholders

64 years 66

years AT

ANNUITIZATION

(INCLUDES

INCOME BENEFIT

GUARANTEES)

Separate

account value \$

1,846 \$ 3,394

Net amount at

risk (2) \$

1,459 \$ 144

Weighted

average waiting

period until

annuitization

options

available 4

years 3 years

FOR CUMULATIVE

PERIODIC

WITHDRAWALS

Separate

account value \$

718 \$ 1,218

Net

amount at risk

(3) \$ 159 \$ 4

ACCUMULATION AT

SPECIFIED DATES

Separate

account value \$

984 \$ 1,587

Net

amount at risk

(4) \$ 223 \$ --

Weighted

average waiting

period until

guarantee date

9 years 10

years

- (1) Defined as the estimated current guaranteed minimum death benefit in excess of the current account balance at the balance sheet date.
- (2) Defined as the estimated present value of the guaranteed minimum annuity payments in excess of the current account balance.
- (3) Defined as the estimated current guaranteed minimum withdrawal balance (initial deposit) in excess of the current account balance at the balance sheet date.
- (4) Defined as the estimated present value of the guaranteed minimum accumulation balance in excess of the current account balance.

The liability for death and income benefit guarantees is equal to a benefit ratio multiplied by the cumulative contract charges earned, plus accrued interest less contract benefit payments. The benefit ratio is calculated as the estimated present value of all expected contract benefits divided by the present value of all expected contract charges. The establishment of reserves for these guarantees requires the projection of future separate account fund performance, mortality, persistency and customer benefit utilization rates. These assumptions

reinsurance	
recoverables (121)	
(26) -- (147) Net	
balance at December	
31, 2007	24 19 -- 43
Incurred guaranteed	
benefits	11 -- -- 11
Paid guarantee	
benefits (1) -- --	
(1) -----	

Net change	10 -- --
10 Net balance at	
December 31, 2008	34
19 -- 53 Plus	
reinsurance	
recoverables	81 200
266 547 -----	

- Balance, December	
31, 2008(3)	\$ 115 \$
219 \$ 266 \$ 600	
=====	
=====	
=====	
=====	

-
- (1) Included in the total liability balance at December 31, 2006 are reserves for variable annuity death benefits of \$89 million, variable annuity income benefits of \$20 million, variable annuity accumulation benefits of \$(7) million, variable annuity withdrawal benefits of \$(1) million and other guarantees of \$52 million.
 - (2) Included in the total liability balance at December 31, 2007 are reserves for variable annuity death benefits of \$111 million, variable annuity income benefits of \$23 million, variable annuity accumulation benefits of \$(0.4) million and other guarantees of \$56 million.
 - (3) Included in the total liability balance at December 31, 2008 are reserves for variable annuity death benefits of \$67 million, variable annuity income benefits of \$200 million, variable annuity accumulation benefits of \$147 million, variable annuity withdrawal benefits of \$119 million and other guarantees of \$67 million.

9. REINSURANCE

The Company reinsures certain of its risks to other insurers primarily under yearly renewable term, coinsurance, and modified coinsurance agreements. These agreements result in a passing of the agreed-upon percentage of risk to the reinsurer in exchange for negotiated reinsurance premium payments. The Company cedes 100% of the morbidity risk on substantially all of its long-term care contracts. The Company cedes specified percentages of the mortality risk on certain life policies, depending upon the issue date and product, to a pool of fourteen unaffiliated reinsurers. Beginning in July 2007, for new life insurance contracts, the Company ceded the mortality risk associated with coverage in excess of \$3 million per life for contracts issued to individuals age 70 and over, and ceded the mortality risk associated with coverage in excess of \$5 million per life for most other contracts. Also beginning in July 2007, for certain large contracts that meet specific criteria, the Company's retention limit was increased to \$10 million per life. In the period prior to July 2007, but subsequent to August 1998, the Company ceded the mortality risk associated with coverage in excess of \$2 million per life, except in 2006 in certain instances when specific criteria were met, it ceded the mortality risk associated with coverage in excess of \$5 million per life. For business sold prior to October 1998, the Company ceded mortality risk in excess of specific amounts up to \$1 million for individual life.

In addition, the Company has used reinsurance to effect the acquisition or disposition of certain blocks of business. The Company had reinsurance recoverables of \$1.57 billion and \$1.26 billion at December 31, 2008 and 2007, respectively, due from Prudential related to the disposal of substantially all of its variable annuity business that was effected through Reinsurance Agreements (see Note 3). In 2008, premiums and contract charges of \$238

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

million, contract benefits of \$467 million, interest credited to contractholder funds of \$36 million, and operating costs and expenses of \$47 million were ceded to Prudential pursuant to the Reinsurance Agreements. In 2007, premiums and contract charges of \$317 million, contract benefits of \$59 million, interest credited to contractholder funds of \$43 million, and operating costs and expenses of \$72 million were ceded to Prudential pursuant to the Reinsurance Agreements. In 2006, premiums and contract charges of \$170 million, contract benefits of \$29 million, interest credited to contractholder funds of \$35 million, and operating costs and expenses of \$64 million were ceded to Prudential pursuant to the Reinsurance Agreements. In addition, as of December 31, 2008 and 2007, the Company had reinsurance recoverables of \$181 million and \$166 million, respectively, due from subsidiaries of Citigroup (Triton Insurance and American Health and Life Insurance), and Scottish Re (U.S.) Inc. in connection with the disposition of substantially all of the direct response distribution business in 2003.

As of December 31, 2008, the gross life insurance in force was \$528.22 billion of which \$249.64 billion was ceded to unaffiliated reinsurers.

The effects of reinsurance on premiums and contract charges for the years ended December 31 are as follows:

(\$ IN MILLIONS)	
2008	2007
2006	-----
-----	-----
-----	-----
PREMIUMS AND CONTRACT CHARGES	
Direct \$	
2,275	\$
2,342	\$
2,326	
Assumed	
Affiliate 70	
16	16 Non-
affiliate 25	
26	30 Ceded-
-non-	
affiliate	
(874)	(940)
(787)	-----
-----	-----
-----	-----
Premiums and contract charges, net of reinsurance	
\$ 1,496	\$
1,444	\$
1,585	
=====	
=====	
=====	

The effects of reinsurance on contract benefits for the years ended December 31 are as follows:

(\$ IN MILLIONS)	
2008	2007
2006	-----
-----	-----
-----	-----
CONTRACT BENEFITS	
Direct \$	
2,428	\$
1,973	\$
1,886	
Assumed	
Affiliate 42	

10 11 Non-
 affiliate 26
 27 23 Ceded-
 -non-
 affiliate
 (1,099)
 (646) (548)

 - -----

 Contract
 benefits,
 net of
 reinsurance
 \$ 1,397 \$
 1,364 \$
 1,372

=====
 =====
 =====

The effects of reinsurance on interest credited to contractholder funds for the years ended December 31 are as follows:

(\$ IN
 MILLIONS)
 2008 2007
 2006 -----

 INTEREST
 CREDITED TO
 CONTRACTHOLDER
 FUNDS Direct
 \$ 2,373 \$
 2,644 \$ 2,534
 Assumed
 Affiliate 11
 13 24 Non-
 affiliate 15
 18 26 Ceded--
 non-affiliate
 (43) (47)
 (41) -----

 Interest
 credited to
 contractholder
 funds, net of
 reinsurance \$
 2,356 \$ 2,628
 \$ 2,534

=====
 =====
 =====

Reinsurance recoverables at December 31 are summarized in the following table.

REINSURANCE
 RECOVERABLE
 ON (\$ IN
 MILLIONS)
 PAID AND
 UNPAID
 BENEFITS --

 --- 2008
 2007 -----

 Annuities \$
 1,734 \$
 1,423 Life
 insurance

1,465 1,365
 Long-term
 care 630
 526 Other
 94 96 -----

 Total \$
 3,923 \$
 3,410
 =====
 =====

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

At December 31, 2008 and 2007, approximately 93% and 88%, respectively, of the Company's reinsurance recoverables are due from companies rated A- or better by S&P.

10. DEFERRED POLICY ACQUISITION AND SALES INDUCEMENT COSTS

Deferred policy acquisition costs for the years ended December 31 are as follows:

	(\$ IN	
	MILLIONS)	
	2008	2007
2006	-----	-----
	-----	-----
	-----	-----
Balance,		
beginning of		
year	\$ 3,905	
	\$ 3,485	\$
	3,948	
Reinsurance		
assumed (1)	32	-- --
Impact of		
adoption of		
SOP 05-1 (2)	--	(11) --
Disposition		
of operation		
(3)	-- --	
	(726)	
Acquisition		
costs		
deferred	596	
	547	742
Amortization		
charged to		
income (643)	(518)	(538)
Effect of		
unrealized		
gains and		
losses	2,811	
	402	59
	-----	-----
	-----	-----
Balance, end		
of year	\$	
	6,701	\$
	3,905	\$
	3,485	
	=====	=====
	=====	=====
	=====	=====

(1) In 2008, DAC increased as a result of a reinsurance transaction with AHL (see Note 5).
 (2) The adoption of SOP 05-1 resulted in an \$11 million adjustment to

unamortized DAC related to the impact on future estimated gross profits from the changes in accounting for certain costs associated with contract continuations that no longer qualify for deferral (see Note 2).

- (3) In 2006, DAC was reduced related to the disposition through reinsurance agreements of substantially all of the Company's variable annuity business (see Note 3).

Net accretion of DAC amortization related to realized capital gains and losses was \$515 million, \$17 million and \$50 million in 2008, 2007 and 2006, respectively.

As disclosed in Note 3, DAC and DSI balances were reduced during 2006 related to the disposal through reinsurance agreements of substantially all of the variable annuity business.

DSI activity, which primarily relates to fixed annuities, for the years ended December 31 was as follows:

(\$ IN MILLIONS)	
2008	2007
2006	-----
-----	-----
-----	-----
Balance, beginning of year	\$ 295
	\$ 225
Impact of adoption of SOP 05-1 (1)	-- (2) --
Disposition of operation (2)	-- (70)
Sales inducements deferred	47
	64
Amortization charged to income	(53)
	(57)
Effect of unrealized gains and losses	164
	65
-----	-----
-----	-----
Balance, end of year	\$ 453
	\$ 295
	\$ 225
=====	=====
=====	=====
=====	=====

- (1) The adoption of SOP 05-1 resulted in a \$2 million adjustment to unamortized DSI related to the impact on future estimated gross profits from the changes in accounting for certain costs associated with contract continuations that no longer qualify for deferral (see Note 2).
- (2) In 2006, DSI was reduced related to the disposition through reinsurance agreements of substantially all of the Company's variable annuity business (see Note 3).

11. COMMITMENTS, GUARANTEES AND CONTINGENT LIABILITIES

GUARANTY FUNDS

Under state insurance guaranty fund laws, insurers doing business in a state can be assessed, up to prescribed limits, for certain obligations of insolvent insurance companies to policyholders and claimants. Amounts assessed to each company are typically related to its proportion of business written in each state. The Company's policy is to accrue a guaranty fund assessment when the entity for which the insolvency relates has been declared financially

insolvent by a court of competent jurisdiction and, in certain states, there is also a final order of liquidation, and the amount of loss is reasonably estimable. As of December 31, 2008 and 2007, the liability balance included in other liabilities and accrued expenses was \$30 million and \$21 million, respectively. The related premium tax offsets included in other assets were \$29 million and \$21 million as of December 31, 2008 and 2007, respectively.

The New York Liquidation Bureau (the "Bureau") has publicly reported that Executive Life Insurance Company of New York ("Executive Life") is currently under its jurisdiction as part of a 1992 court-ordered

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

rehabilitation plan and may only be able to meet future obligations of its annuity contracts for the next fifteen years. However, Executive Life does not have a liquidity problem at this time, and an order of liquidation has not been sought by the Bureau. The shortfall was estimated by the Bureau to be \$1.27 billion at October 29, 2008.

If Executive Life were to be declared insolvent in the future, the Company may have exposure to future guaranty fund assessments. The Company's exposure will ultimately depend on the level of guaranty fund system participation, as well as the viability of a plan of the Bureau to obtain voluntary contributions, primarily from the original insurance companies that acquired structured settlement annuity contracts from Executive Life. Under current law, the Company may be allowed to recoup a portion of the amount of any additional guaranty fund assessment in periods subsequent to the recognition of the assessment by offsetting future premium taxes. The Company's New York market share was approximately 4.1% in 2007 based on industry annuity premium.

GUARANTEES

The Company owns certain fixed income securities that obligate the Company to exchange credit risk or to forfeit principal due, depending on the nature or occurrence of specified credit events for the referenced entities. In the event all such specified credit events were to occur, the Company's maximum amount at risk on these fixed income securities, as measured by the amount of the aggregate initial investment was \$195 million at December 31, 2008. The obligations associated with these fixed income securities expire at various dates during the next six years.

In the normal course of business, the Company provides standard indemnifications to contractual counterparties in connection with numerous transactions, including acquisitions and divestitures. The types of indemnifications typically provided include indemnifications for breaches of representations and warranties, taxes and certain other liabilities, such as third party lawsuits. The indemnification clauses are often standard contractual terms and are entered into in the normal course of business based on an assessment that the risk of loss would be remote. The terms of the indemnifications vary in duration and nature. In many cases, the maximum obligation is not explicitly stated and the contingencies triggering the obligation to indemnify have not occurred and are not expected to occur. Consequently, the maximum amount of the obligation under such indemnifications is not determinable. Historically, the Company has not made any material payments pursuant to these obligations.

The aggregate liability balance related to all guarantees was not material as of December 31, 2008.

REGULATION

The Company is subject to changing social, economic and regulatory conditions. From time to time, regulatory authorities or legislative bodies seek to impose additional regulations regarding agent and broker compensation and otherwise expand overall regulation of insurance products and the insurance industry. The ultimate changes and eventual effects of these initiatives on the Company's business, if any, are uncertain.

LEGAL AND REGULATORY PROCEEDINGS AND INQUIRIES

BACKGROUND

The Company and certain affiliates are involved in a number of lawsuits, regulatory inquiries, and other legal proceedings arising out of various aspects of its business. As background to the "Proceedings" subsection below, please note the following:

- These matters raise difficult and complicated factual and legal issues

and are subject to many uncertainties and complexities, including the underlying facts of each matter; novel legal issues; variations between jurisdictions in which matters are being litigated, heard, or investigated; differences in applicable laws and judicial interpretations; the length of time before many of these matters might be resolved by settlement, through litigation or otherwise; the fact that some of the lawsuits are putative class actions in which a class has not been certified and in which the purported class may not be clearly defined; the fact that some of the lawsuits involve multi-state class actions in which the applicable law(s) for the claims at issue is in dispute and therefore unclear; and the current challenging legal environment faced by large corporations and insurance companies.

- The outcome on these matters may also be affected by decisions, verdicts, and settlements, and the timing of such decisions, verdicts, and settlements, in other individual and class action lawsuits that involve the Company, other insurers, or other entities and by other legal, governmental, and regulatory actions that involve the Company, other insurers, or other entities.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

- In the lawsuits, plaintiffs seek a variety of remedies including equitable relief in the form of injunctive and other remedies and monetary relief in the form of contractual and extra-contractual damages. In some cases, the monetary damages sought include punitive damages. Often specific information about the relief sought, such as the amount of damages, is not available because plaintiffs have not requested specific relief in their pleadings. In the Company's experience, when specific monetary demands are made in pleadings, they bear little relation to the ultimate loss, if any, to the Company.
- In connection with regulatory examinations and proceedings, government authorities may seek various forms of relief, including penalties, restitution and changes in business practices. The Company may not be advised of the nature and extent of relief sought until the final stages of the examination or proceeding.
- For the reasons specified above, it is often not possible to make meaningful estimates of the amount or range of loss that could result from the matters described below in the "Proceedings" subsection. The Company reviews these matters on an ongoing basis and follows the provisions of SFAS No. 5, "Accounting for Contingencies", when making accrual and disclosure decisions. When assessing reasonably possible and probable outcomes, the Company bases its decisions on its assessment of the ultimate outcome following all appeals.
- Due to the complexity and scope of the matters disclosed in the "Proceedings" subsection below and the many uncertainties that exist, the ultimate outcome of these matters cannot be reasonably predicted. In the event of an unfavorable outcome in one or more of these matters, the ultimate liability may be in excess of amounts currently reserved and may be material to the Company's operating results or cash flows for a particular quarterly or annual period. However, based on information currently known to it, management believes that the ultimate outcome of all matters described below, as they are resolved over time, is not likely to have a material adverse effect on the financial position of the Company.

PROCEEDINGS

Legal proceedings involving Allstate agencies and AIC may impact the Company, even when the Company is not directly involved, because the Company sells its products through a variety of distribution channels including Allstate agencies. Consequently, information about the more significant of these proceedings is provided in the following paragraph.

AIC is defending certain matters relating to its agency program reorganization announced in 1999. These matters are in various stages of development.

- These matters include a lawsuit filed in 2001 by the U.S. Equal Employment Opportunity Commission ("EEOC") alleging retaliation under federal civil rights laws (the "EEOC I" suit) and a class action filed in 2001 by former employee agents alleging retaliation and age discrimination under the Age Discrimination in Employment Act ("ADEA"), breach of contract and ERISA violations (the "Romero I" suit). In 2004, in the consolidated EEOC I and Romero I litigation, the trial court

issued a memorandum and order that, among other things, certified classes of agents, including a mandatory class of agents who had signed a release, for purposes of effecting the court's declaratory judgment that the release is voidable at the option of the release signer. The court also ordered that an agent who voids the release must return to AIC "any and all benefits received by the [agent] in exchange for signing the release." The court also stated that, "on the undisputed facts of record, there is no basis for claims of age discrimination." The EEOC and plaintiffs have asked the court to clarify and/or reconsider its memorandum and order and in January 2007, the judge denied their request. In June 2007, the court granted AIC's motions for summary judgment. Following plaintiffs' filing of a notice of appeal, the Third Circuit issued an order in December 2007 stating that the notice of appeal was not taken from a final order within the meaning of the federal law and thus not appealable at this time. In March 2008, the Third Circuit decided that the appeal should not summarily be dismissed and that the question of whether the matter is appealable at this time will be addressed by the Court along with the merits of the appeal.

- The EEOC also filed another lawsuit in 2004 alleging age discrimination with respect to a policy limiting the rehire of agents affected by the agency program reorganization (the "EEOC II" suit). In EEOC II, in 2006, the court granted partial summary judgment to the EEOC. Although the court did not determine that AIC was liable for age discrimination under the ADEA, it determined that the rehire policy resulted in a disparate impact, reserving for trial the determination on whether AIC had reasonable factors other than age

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

to support the rehire policy. AIC's interlocutory appeal from the partial summary judgment was granted. In June 2008, the Eighth Circuit Court of Appeals affirmed summary judgment in the EEOC's favor. In September 2008, the Court of Appeals granted AIC's petition for rehearing EN BANC and vacated its earlier decision affirming the trial court's grant of summary judgment in favor of the EEOC. The Court of Appeals then dismissed the appeal, determining that it lacked jurisdiction to consider the appeal at this stage in the litigation.

- AIC is also defending a certified class action filed by former employee agents who terminated their employment prior to the agency program reorganization. Plaintiffs allege that they were constructively discharged so that AIC could avoid paying ERISA and other benefits offered under the reorganization. They claim that the constructive discharge resulted from the implementation of agency standards, including mandatory office hours and a requirement to have licensed staff available during business hours. The court approved the form of class notice which was sent to approximately 1,800 potential class members in November 2007. Fifteen individuals opted out. AIC's motions for judgment on the pleadings were partially granted. In May 2008, the court granted summary judgment in AIC's favor on all class claims. Plaintiffs moved for reconsideration and in the alternative to decertify the class. AIC opposed this motion and filed a motion for summary judgment with respect to the remaining non-class claim. In August 2008, the court denied plaintiffs' motion to reconsider and to decertify the class. In February 2009, plaintiffs moved to dismiss the sole remaining claim with prejudice which the court promptly granted ending this litigation in the trial court.
- A putative nationwide class action has also been filed by former employee agents alleging various violations of ERISA, including a worker classification issue. These plaintiffs are challenging certain amendments to the Agents Pension Plan and are seeking to have exclusive agent independent contractors treated as employees for benefit purposes. This matter was dismissed with prejudice by the trial court, was the subject of further proceedings on appeal, and was reversed and remanded to the trial court in 2005. In June 2007, the court granted AIC's motion to dismiss the case. Following plaintiffs' filing of a notice of appeal, the Third Circuit issued an order in December 2007 stating that the notice of appeal was not taken from a final order within the meaning of the federal law and thus not appealable at this time. In March 2008, the Third Circuit decided that the appeal should not summarily be dismissed and that the question of whether the matter is appealable at this time will be addressed by the Court along with the merits of the appeal.

In all of these various matters, plaintiffs seek compensatory and punitive damages, and equitable relief. AIC has been vigorously defending these lawsuits and other matters related to its agency program reorganization.

OTHER MATTERS

Various other legal, governmental, and regulatory actions, including state market conduct exams, and other governmental and regulatory inquiries are currently pending that involve the Company and specific aspects of its conduct of business. Like other members of the insurance industry, the Company is the target of a number of class action lawsuits and other types of proceedings, some of which involve claims for substantial or indeterminate amounts. These actions are based on a variety of issues and target a range of the Company's practices. The outcome of these disputes is currently unpredictable.

One or more of these matters could have an adverse effect on the Company's operating results or cash flows for a particular quarterly or annual period. However, based on information currently known to it, management believes that the ultimate outcome of all matters described in this "Other Matters" subsection, in excess of amounts currently reserved, as they are resolved over time is not likely to have a material effect on the operating results, cash flows or financial position of the Company.

12. INCOME TAXES

ALIC and its domestic subsidiaries (the "Allstate Life Group") join with the Corporation (the "Allstate Group") in the filing of a consolidated federal income tax return and are party to a federal income tax allocation agreement (the "Allstate Tax Sharing Agreement"). Under the Allstate Tax Sharing Agreement, the Allstate Life Group pays to or receives from the Corporation the amount, if any, by which the Allstate Group's federal income tax liability is affected by virtue of inclusion of the Allstate Life Group in the consolidated federal income tax return. Effectively, this results in the Allstate Life Group's annual income tax provision being computed, with adjustments, as if the Allstate Life Group filed a separate return.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Internal Revenue Service ("IRS") is currently examining the Allstate Group's 2005 and 2006 federal income tax returns. The statute of limitations has expired on years prior to 2005. Any adjustments that may result from IRS examinations of tax returns are not expected to have a material effect on the results of operations, cash flows or financial position of the Company.

The Company had no liability for unrecognized tax benefits at December 31, 2008 or 2007 or January 1, 2007, and believes it is reasonably possible that the liability balance will not significantly increase within the next twelve months. No amounts have been accrued for interest or penalties.

The components of the deferred income tax assets and liabilities at December 31 are as follows:

(\$ IN
MILLIONS)
2008 2007 -

- DEFERRED
ASSETS Life
and annuity
reserves \$
306 \$ 588
Unrealized
net capital
losses
1,254 45
Difference
in tax
bases of
investments
381 23 Net
operating
loss
carryforward
208 --
Other
assets 43
39 -----

Total

```

deferred
assets
2,192 695
Valuation
allowance
(9) -- ----
-----
-----
Net
deferred
assets
2,183 695
DEFERRED
LIABILITIES
DAC (790)
(787) Other
liabilities
(11) (9) --
-----
-----
- Total
deferred
liabilities
(801) (796)
-----
-----
--- Net
deferred
asset
(liability)
$ 1,382 $
(101)
=====
=====

```

Although realization is not assured, management believes it is more likely than not that the deferred tax assets, net of valuation allowance, will be realized based on the Company's assessment that the deductions ultimately recognized for tax purposes will be able to be fully utilized. The valuation allowance for deferred tax assets increased by \$9 million in 2008.

The components of income tax (benefit) expense for the years ended December 31 are as follows:

```

($ IN
MILLIONS)
2008 2007
2006 -----
-----
-----
Current $
(640) $ 111
$ 136
Deferred
(including
$208
million tax
benefit of
operating
loss
carryforward
in 2008)
(306) 69 60
-----
-----
-----
----- Total
income tax
(benefit)
expense $
(946) $ 180
$ 196
=====
=====
=====

```

As of December 31, 2008, the Company has a net operating loss carryforward of approximately \$593 million, which will be available to offset future taxable

income. This carryforward will expire at the end of 2023.

The Company received an income tax refund of \$118 million in 2008. The Company paid income taxes of \$68 million and \$317 million in 2007 and 2006, respectively. The Company had a current income tax receivable of \$529 million and \$6 million at December 31, 2008 and 2007, respectively.

A reconciliation of the statutory federal income tax rate to the effective income tax rate on income from operations for the years ended December 31 is as follows:

2008	2007
2006	-----
-----	-----
-----	-----
-----	-----
Statutory federal income tax rate - (benefit) expense (35.0) %	
35.0 %	35.0 %
% Dividends received deduction (0.5)	(2.7)
(2.7) Tax credits (0.2)	(2.3)
(0.5) Other (0.2)	0.4
(0.5)	-----
-----	-----
-----	-----
Effective income tax rate - (benefit) expense (35.9) %	
30.4 %	31.3 %
=====	
=====	
=====	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

13. CAPITAL STRUCTURE

DEBT OUTSTANDING

All of the Company's outstanding debt as of December 31, 2008 and 2007 relates to intercompany obligations. These obligations reflect surplus notes due to related parties and are discussed in Note 5 to the consolidated financial statements. The Company paid \$13 million, \$21 million and \$13 million of interest on debt in 2008, 2007 and 2006, respectively.

14. STATUTORY FINANCIAL INFORMATION

ALIC and its subsidiaries prepare their statutory-basis financial statements in conformity with accounting practices prescribed or permitted by the insurance department of the applicable state of domicile. Prescribed statutory accounting practices include a variety of publications of the NAIC, as well as state laws, regulations and general administrative rules. Permitted statutory accounting practices encompass all accounting practices not so prescribed.

All states require domiciled insurance companies to prepare statutory-basis financial statements in conformity with the NAIC Accounting Practices and Procedures Manual, subject to any deviations prescribed or permitted by the applicable insurance commissioner and/or director.

Statutory accounting practices differ from GAAP primarily since they

require charging policy acquisition and certain sales inducement costs to expense as incurred, establishing life insurance reserves based on different actuarial assumptions, and valuing certain investments and establishing deferred taxes on a different basis.

Statutory net (loss) income of ALIC and its insurance subsidiaries for 2008, 2007 and 2006 was \$(1.98) billion, \$172 million and \$252 million, respectively. Statutory capital and surplus was \$3.25 billion and \$2.62 billion as of December 31, 2008 and 2007, respectively.

The commissioner of the Illinois Division of Insurance has permitted ALIC to record its market value adjusted annuity assets and liabilities at book value pursuant to the Illinois Insurance Code which provides an alternative from market value accounting with approval of the commissioner. This accounting practice would have increased statutory capital and surplus by \$394 million as of October 1, 2008. On a pro-forma basis, this accounting practice increased statutory capital and surplus by \$1.24 billion at December 31, 2008 over what it would have been had the permitted practice not been allowed. The increase from October 1, 2008 was primarily the result of decreases in the fair value of the investments, while the reserve balances were comparable.

The commissioner of the Illinois Division of Insurance has permitted ALIC to admit deferred tax assets that are expected to be realized within three years of the balance sheet date limited to 15% of statutory capital and surplus, instead of deferred tax assets that are expected to be realized within one year of the balance sheet date limited to 10% of statutory capital and surplus. This accounting practice increased statutory capital and surplus by \$140 million at December 31, 2008 over what it would have been had the permitted practice not been allowed. Admitted statutory-basis deferred tax assets totaled \$421 million or 52% of the gross deferred tax assets before non-admission limitations.

DIVIDENDS

The ability of ALIC to pay dividends is dependent on business conditions, income, cash requirements of ALIC, receipt of dividends from its subsidiaries and other relevant factors. The payment of shareholder dividends by ALIC to AIC without the prior approval of the state insurance regulator is limited to formula amounts based on net income and capital and surplus, determined in conformity with statutory accounting practices, as well as the timing and amount of dividends paid in the preceding twelve months. The amount of dividends is further limited to the amount of unassigned funds, which is the portion of statutory capital and surplus out of which dividends can be paid. Notification and approval of intercompany lending activities is also required by the Illinois Division of Insurance ("IL DOI") for transactions that exceed a level that is based on a formula using statutory admitted assets and statutory surplus.

ALIC paid no dividends in 2008 and paid dividends of \$725 million in 2007. The 2007 dividends were in excess of the \$336 million that was allowed under Illinois insurance law based on the 2006 formula amount. ALIC received approval from the IL DOI for the portion of the 2007 dividends in excess of this amount. Based on ALIC's statutory capital and surplus, the maximum amount of dividends ALIC will be able to pay without prior IL DOI

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

approval at a given point in time during 2009 is \$325 million, less dividends paid during the preceding twelve months measured at that point in time. This value is further limited by the amount of unassigned funds at that point in time. As of December 31, 2008, ALIC's unassigned funds was \$136 million.

15. BENEFIT PLANS

PENSION AND OTHER POSTRETIREMENT PLANS

Defined benefit pension plans, sponsored by AIC, cover most full-time employees, certain part-time employees and employee-agents. Benefits under the pension plans are based upon the employee's length of service and eligible annual compensation. A cash balance formula was added to the Allstate Retirement Plan effective January 1, 2003. All eligible employees hired before August 1, 2002 were provided with a one-time opportunity to choose between the cash balance formula and the final average pay formula. The cash balance formula applies to all eligible employees hired after August 1, 2002. AIC's funding policy for the pension plans is to make annual contributions at a minimum level that is at least in accordance with regulations under the Internal Revenue Code and in accordance with generally accepted actuarial principles. The allocated cost to the Company included in net income for the pension plans in 2008, 2007 and 2006 was \$16 million, \$24 million and \$37 million, respectively.

AIC also provides certain health care and life insurance subsidies for employees hired before January 1, 2003 when they retire ("postretirement benefits"). Qualified employees may become eligible for these benefits if they retire in accordance with AIC's established retirement policy and are continuously insured under AIC's group plans or other approved plans in accordance with the plan's participation requirements. AIC shares the cost of the retiree medical benefits with retirees based on years of service, with AIC's share being subject to a 5% limit on annual medical cost inflation after retirement. AIC has the right to modify or terminate these pension and postretirement benefit plans. The allocated cost to the Company included in net income was \$4 million, \$6 million and \$7 million for postretirement benefits other than pension plans in 2008, 2007 and 2006, respectively.

ALLSTATE 401(k) SAVINGS PLAN

Employees of AIC are eligible to become members of the Allstate 401(k) Savings Plan. The Corporation's contributions are based on the Corporation's matching obligation and certain performance measures. The Company's allocation of profit sharing expense from the Corporation was \$6 million, \$12 million and \$13 million in 2008, 2007 and 2006, respectively.

16. OTHER COMPREHENSIVE LOSS

The components of other comprehensive loss on a pre-tax and after-tax basis for the years ended December 31 are as follows:

(\$ IN MILLIONS)
2008 2007 2006

	2008	2007	2006
PRE-TAX			
AFTER-TAX			
Unrealized net holding losses arising during the period, net of related offsets	\$ (5,525)	\$ 1,925	\$ (3,600)
Less: reclassification adjustment of realized capital gains and losses	(2,072)	725	(1,347)
	(48)	89	(89)
	(58)		
Unrealized net capital gains and losses	(3,453)	1,200	(2,253)
	220	(409)	(404)
	141	(263)	

 Other
 comprehensive
 loss \$ (3,453)
 \$ 1,200 \$
 (2,253) \$ (629)
 \$ 220 \$ (409) \$
 (404) \$ 141 \$
 (263) =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====
 =====

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

17. QUARTERLY RESULTS (UNAUDITED)

FIRST
 QUARTER
 SECOND
 QUARTER
 THIRD
 QUARTER
 FOURTH
 QUARTER

--- (\$
 IN
 MILLIONS)
 2008
 2007
 2008
 2007
 2008
 2007
 2008
 2007
 2008
 2007 ---

Revenues
 \$ 916 \$
 1,435 \$
 362 \$
 1,509 \$
 710 \$
 1,274 \$
 176 \$
 1,234
 Net
 (loss)
 income
 (115)
 149
 (368)
 187
 (184) 56

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

TO THE BOARD OF DIRECTORS AND SHAREHOLDER OF
ALLSTATE LIFE INSURANCE COMPANY

We have audited the accompanying Consolidated Statements of Financial Position of Allstate Life Insurance Company and subsidiaries (the "Company", an affiliate of The Allstate Corporation) as of December 31, 2008 and 2007, and the related Consolidated Statements of Operations and Comprehensive Income, Shareholder's Equity, and Cash Flows for each of the three years in the period ended December 31, 2008. Our audits also included the consolidated financial statement schedules listed in the Index at Item 15. These financial statements and financial statement schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedules based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Allstate Life Insurance Company and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2008, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such consolidated financial statement schedules, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly in all material respects the information set forth therein.

As discussed in Note 2 to the consolidated financial statements, the Company changed its method of accounting for uncertainty in income taxes and accounting for deferred acquisition costs associated with internal replacements in 2007.

/s/ Deloitte & Touche LLP

Chicago, Illinois
March 17, 2009

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES. We maintain disclosure controls and procedures as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934. Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based upon this evaluation, the principal executive officer and the principal financial officer concluded that our disclosure controls and procedures are effective in providing reasonable assurance that material information required to be disclosed in our reports filed with or submitted to the Securities and Exchange Commission under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities Exchange Act and made known to management, including the

principal executive officer and the principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING.

Management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting as of December 31, 2008 based on the criteria related to internal control over financial reporting described in "Internal Control - Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation, management concluded that our internal control over financial reporting was effective as of December 31, 2008.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING. During the fiscal quarter ended December 31, 2008, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

(1), (2), (3) AND (4) DISCLOSURE OF FEES -

The following fees have been, or are anticipated to be billed by Deloitte & Touche LLP, the member firms of Deloitte & Touche Tohmatsu, and their respective affiliates, for professional services rendered to us for the fiscal years ending December 31, 2008 and 2007.

2008	2007	(d) -
-----	-----	-----
-	-	-
-	-	-
-	-	-
(a)	\$ 3,429,870	
	\$ 3,577,888	
	Audit related	
	fees (b)	
	291,806	87,353
	All other fees	
	(c) 40,000	
	45,870	-----
	-----	-----
	-----	-----
	TOTAL	
	FEES \$	
	3,761,676	\$
	3,711,111	
	=====	
	=====	

- (a) Fees for audits of annual financial statements, reviews of quarterly financial statements, statutory audits, attest services, comfort letters, consents and review of documents filed with the Securities and Exchange Commission.
- (b) Audit related fees relate primarily to professional services such as accounting consultations relating to new accounting standards.

2008 2007 ---

Adoption of

new
 accounting
 standards \$
 152,132 \$
 57,353
 Investment
 related
 research
 65,236 --
 Other 74,438
 30,000 -----

 AUDIT RELATED
 FEES \$
 291,806 \$
 87,353
 =====
 =====

(c) All other fees relate to benchmarking studies and coordination of work for departments of insurance exams.

(d) Total fees for 2007 have been adjusted to add an additional \$314,798 of fees and to reclassify certain fees to conform to the current year presentation. The \$314,798 is primarily comprised of audit fees not charged until 2008.

(5)(i) AND (ii) AUDIT COMMITTEE'S PRE-APPROVAL POLICIES AND PROCEDURES -

The Audit Committee of The Allstate Corporation has established pre-approval policies and procedures for itself and its consolidated subsidiaries, including Allstate Life. Those policies and procedures are incorporated into this Item 14 (5) by reference to Exhibit 99 - The Allstate Corporation Policy Regarding Pre-Approval of Independent Registered Public Accountant's Services (the "Pre-Approval Policy"). In addition, in 2005 the Audit Committee of Allstate Life adopted the Pre-Approval Policy, as it may be amended from time to time by the Audit Committee or the Board of Directors of the Corporation, as its own policy, provided that the Designated Member referred to in such policy need not be independent because the New York Stock Exchange corporate governance standards do not apply to Allstate Life. All of the services provided by Deloitte & Touche LLP to Allstate Life in 2007 and 2008 were approved by The Allstate Corporation and Allstate Life Audit Committees.

PART IV

ITEM 15. (a) (1) EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

The following consolidated financial statements, notes thereto and related information of Allstate Life Insurance Company are included in Item 8.

- Consolidated Statements of Operations and Comprehensive Income
- Consolidated Statements of Financial Position
- Consolidated Statements of Shareholder's Equity
- Consolidated Statements of Cash Flows
- Notes to the Consolidated Financial Statements
- Report of Independent Registered Public Accounting Firm

ITEM 15. (a) (2)

The following additional financial statement schedules and independent auditors' report are furnished herewith pursuant to the requirements of Form 10-K.

ALLSTATE
 LIFE
 INSURANCE
 COMPANY
 PAGE
 Schedules
 required
 to be
 filed
 under the
 provisions
 of
 Regulation
 S-X

Article 7:
Schedule I
- Summary
of
Investments
- Other
than
Investments
in Related
Parties S-
1 Schedule
IV -
Reinsurance
S-2
Schedule V
-
Valuation
Allowances
and
Qualifying
Accounts
S-3

All other schedules are omitted because they are not applicable, or not required, or because the required information is included in the Consolidated Financial Statements or notes thereto.

ITEM 15. (a) (3)

The following is a list of the exhibits filed as part of this Form 10-K. The SEC File Number for the exhibits incorporated by reference is 000-31248 except as otherwise noted.

EXHIBIT NO.
DOCUMENT
DESCRIPTION

3(i)
Articles of
Amendment to
the Articles
of
Incorporation
of Allstate
Life
Insurance
Company
dated
December 29,
1999.
Incorporated
herein by
reference to
Exhibit 3.1
to Allstate
Life
Insurance
Company's
Form 10
filed on
April 24,
2002. 3(ii)
Amended and
Restated By-
Laws of
Allstate
Life
Insurance
Company
effective
March 15,
2007.
Incorporated
herein by
reference to
Exhibit
3(ii) to
Allstate

Life
Insurance
Company's
Current
Report on
Form 8-K
filed March
20, 2007. 4
See Exhibits
3 (i) and 3
(ii). 10.1
Form of
Amended and
Restated
Service and
Expense
Agreement
between
Allstate
Insurance
Company, The
Allstate
Corporation
and certain
affiliates
effective
January 1,
2004.
Incorporated
herein by
reference to
Exhibit 10.1
to Allstate
Life
Insurance
Company's
Annual
Report on
Form 10-K
for 2007.
10.2 Letter
Agreement
between
Allstate
Insurance
Company, The
Allstate
Corporation
and certain
affiliates,
including
Allstate
Life
Insurance
Company,
effective
December 1,
2007.
Incorporated
herein by
reference to
Exhibit 10.1
to Allstate
Life
Insurance
Company's
Current
Report on
Form 8-K
filed May
23, 2008.

Company, effective March 5, 2005. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended June 30, 2005.

- 10.4 Selling Agreement between Allstate Life Insurance Company, ALFS, Inc. (f/k/a Allstate Life Financial Services, Inc.) and Allstate Financial Services, LLC (f/k/a LSA Securities, Inc.) effective July 26, 1999. Incorporated herein by reference to Exhibit 10.6 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
- 10.5 Amendment effective August 1, 1999 to Selling Agreement between Allstate Life Insurance Company, ALFS, Inc. and Allstate Financial Services, LLC effective July 26, 1999. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2004.
- 10.6 Amendment effective September 28, 2001 to Selling Agreement between Allstate Life Insurance Company, ALFS, Inc. and Allstate Financial Services, LLC effective July 26, 1999. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2004.
- 10.7 Amendment effective February 15, 2002 to Selling Agreement between Allstate Life Insurance Company, ALFS, Inc. and Allstate Financial Services, LLC effective July 26, 1999. Incorporated herein by reference to Exhibit 10.3 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2004.
- 10.8 Amendment effective April 21, 2003 to Selling Agreement between Allstate Life Insurance Company, ALFS, Inc. and Allstate Financial Services, LLC effective July 26, 1999. Incorporated herein by reference to Exhibit 10.4 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2004.
- 10.9 Selling Agreement between Allstate Life Insurance Company of New York, ALFS, Inc. and Allstate Financial Services, LLC effective May 1, 2005. Incorporated herein by reference to Exhibit 10.7 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
- 10.10 Selling Agreement between Lincoln Benefit Life Company, ALFS, Inc. (f/k/a Allstate Life Financial Services, Inc.) and Allstate Financial Services, LLC (f/k/a LSA Securities, Inc.) effective August 2, 1999. Incorporated herein by reference to Exhibit 10.8 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
- 10.11 First Amendment to Marketing Coordination and Administrative Services Agreement among Allstate Life Insurance Company, Allstate Financial Services, LLC and Allstate Insurance Company dated January 1, 2006. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2006.
- 10.12 Marketing Coordination and Administrative Services Agreement among Allstate Insurance Company, Allstate Life Insurance Company and Allstate Financial Services, LLC effective January 1, 2003. Incorporated herein by reference to Exhibit 10.9 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
- 10.13 Form of Investment Management Agreement among Allstate Investments, LLC, Allstate Insurance Company, The Allstate Corporation and certain affiliates effective January 1, 2007. Incorporated herein by reference to Exhibit 10.12 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
- 10.14 Investment Advisory Agreement by and between Allstate Insurance Company and Intramerica Life Insurance Company effective July 1, 1999. Incorporated herein by reference to Exhibit 10.29 to Allstate Life Insurance Company's Form 10 filed on April 24, 2002.
- 10.15 Investment Management Agreement between Allstate Investments, LLC and ALIC Reinsurance Company, effective July 1, 2005. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2005.
- 10.16 Assignment and Assumption Agreement dated as of January 1, 2002 among Allstate Insurance Company, Allstate Investments, LLC and Intramerica Life Insurance Company. Incorporated herein by reference to Exhibit 10.30 to Allstate Life

Insurance Company's Form 10 filed on April 24, 2002.

- 10.17 Investment Advisory Agreement and Amendment to Service Agreement as of January 1, 2002 between Allstate Insurance Company, Allstate Investments, LLC and Allstate Life Insurance Company of New York. Incorporated herein by reference to Exhibit 10.31 to Allstate Life Insurance Company's Form 10 filed on April 24, 2002.
- 10.18 Cash Management Services Master Agreement between Allstate Insurance Company and Allstate Bank (f/k/a Allstate Federal Savings Bank) dated March 16, 1999. Incorporated herein by reference to Exhibit 10.32 to Allstate Life Insurance Company's Form 10 filed on April 24, 2002.
- 10.19 Amendment No. 1 effective January 5, 2001 to Cash Management Services Master Agreement between Allstate Insurance Company and Allstate Bank dated March 16, 1999. Incorporated herein by reference to Exhibit 10.33 to Allstate Life Insurance Company's Form 10 filed on April 24, 2002.
- 10.20 Amendment No. 2 entered into November 8, 2002 to the Cash Management Services Master Agreement between Allstate Insurance Company, Allstate Bank and Allstate Motor Club, Inc. dated March 16, 1999. Incorporated herein by reference to Exhibit 10.19 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.21 Premium Depository Service Supplement dated as of September 30, 2005 to Cash Management Services Master Agreement between Allstate Insurance Company, Allstate Bank, Allstate Motor Club, Inc. and certain other parties. Incorporated herein by reference to Exhibit 10.20 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.22 Variable Annuity Service Supplement dated November 10, 2005 to Cash Management Services Agreement between Allstate Bank, Allstate Life Insurance Company of New York and certain other parties. Incorporated herein by reference to Exhibit 10.21 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.23 Sweep Agreement Service Supplement dated as of October 11, 2006 to Cash Management Services Master Agreement between Allstate Life Insurance Company, Allstate Bank, Allstate Motor Club, Inc. and certain other companies. Incorporated herein by reference to Exhibit 10.22 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.24 Agent Access Agreement among Allstate Insurance Company, Allstate New Jersey Insurance Company, Allstate Life Insurance Company and Allstate Bank effective January 1, 2002. Incorporated herein by reference to Exhibit 10.17 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
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- 10.25 Form of Tax Sharing Agreement among The Allstate Corporation and certain affiliates dated as of November 12, 1996. Incorporated herein by reference to Exhibit 10.24 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.26 Surplus Note Purchase Agreement between Allstate Life Insurance Company and Kennett Capital, Inc. effective, August 1, 2005. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2005.
- 10.27 Intercompany Loan Agreement among The Allstate Corporation, Allstate Life Insurance Company, Lincoln Benefit Life Company and other certain subsidiaries of The Allstate Corporation dated February 1, 1996. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2006.
- 10.28 Pledge and Security Agreement between Allstate Life Insurance Company and Kennett Capital, Inc. effective August 1, 2005. Incorporated herein by reference to Exhibit 10.3 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for quarter ended September 30, 2005.
- 10.29 Catastrophe Reinsurance Agreement between Allstate Life Insurance Company and American Heritage Life Insurance Company effective July 1, 2003. Incorporated herein by reference to Exhibit 10.29 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2003.
- 10.30 Retrocessional Reinsurance Agreement between Allstate Life Insurance Company and American Heritage Life Insurance Company effective December 31, 2004.

Incorporated herein by reference to Exhibit 10.23 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2004.

- 10.31 Reinsurance Agreement between Allstate Life Insurance Company and American Heritage Life Insurance Company effective December 31, 2004. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Current Report on Form 8-K filed January 9, 2008.
- 10.32 Amendment No. 1 to Reinsurance Agreement between Allstate Life Insurance Company and American Heritage Life Insurance Company dated January 1, 2008. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed January 9, 2008.
- 10.33 Credit Agreement dated May 8, 2007, among The Allstate Corporation, Allstate Insurance Company and Allstate Life Insurance Company, as Borrowers; the Lenders party thereto, Wells Fargo Bank, National Association, as Syndication Agent; Bank of America, N.A. and Citibank, N.A., as Documentation Agents; Barclays Bank, PLC, Morgan Stanley Bank and William Street Commitment Corporation, as Co-Agents; and JPMorgan Chase Bank, N.A., as Administrative Agent. Incorporated herein by reference to Exhibit 10.1 to The Allstate Corporation's Current Report on Form 8-K filed May 9, 2007. (SEC File No. 001-11840)
- 10.34 Amendment No. 1 to Credit Agreement dated as of May 22, 2008. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed May 27, 2008.
- 10.35 Reinsurance and Administrative Services Agreement between American Heritage Life Insurance Company and Columbia Universal Life Insurance Company effective February 1, 1998. Incorporated herein by reference to Exhibit 10.3 to Allstate Life Insurance Company's Current Report on Form 8-K filed January 30, 2008.

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- 10.36 Novation and Assignment Agreement among Allstate Life Insurance Company, American Heritage Life Insurance Company and Columbia Universal Life Insurance Company effective June 30, 2004. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Current Report on Form 8-K filed January 30, 2008.
- 10.37 Amendment to Reinsurance Agreement effective December 1, 2007, between American Heritage Life Insurance Company and Allstate Life Insurance Company. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed January 30, 2008.
- 10.38 Capital Support Agreement between Allstate Life Insurance Company and Allstate Insurance Company effective December 14, 2007. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed February 7, 2008.
- 10.39 Amended and Restated Intercompany Liquidity Agreement between Allstate Insurance Company, Allstate Life Insurance Company and The Allstate Corporation effective as of May 8, 2008. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2008.
- 10.40 Agreement for the Settlement of State and Local Tax Credits among Allstate Insurance Company and certain of its affiliates, including Allstate Life Insurance Company effective January 1, 2007. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed February 21, 2008.
- 10.41 Selling Agreement and Addenda to Agreement between Allstate Life Insurance Company as successor in interest to Glenbrook Life and Annuity Company, ALFS, Inc. and Allstate Financial Services, LLC effective May 17, 2001, December 31, 2001 and November 18, 2002, respectively. Incorporated herein by reference to Exhibit 10.39 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.42 Limited Servicing Agreement between Allstate Life Insurance Company, Allstate Distributors, L.L.C. and Allstate Financial Services, LLC effective October 1, 2002. Incorporated herein by reference to Exhibit 10.40 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.
- 10.43 Marketing Agreement between Allstate Life Insurance Company as successor in interest to Glenbrook Life and Annuity Company, ALFS, Inc. and Allstate Financial Services, LLC effective June 10, 2003. Incorporated herein by

reference to Exhibit 10.41 to Allstate Life Insurance Company's Annual Report on Form 10-K for 2007.

- 10.44 Investment Sub-Advisory Agreement between Allstate Institutional Advisors, LLC and Allstate Investment Management Company effective as of March 30, 2008. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed April 24, 2008.
- 10.45 Sale Agreement between Allstate Insurance Company and Allstate Life Insurance Company effective September 10, 2008 for those securities listed on attached Exhibit A. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed September 16, 2008.
- 10.46 Sale Agreement between Allstate Insurance Company and Allstate Life Insurance Company effective September 10, 2008 for those mortgages listed on attached Exhibit A. Incorporated herein by reference to Exhibit 10.2 to Allstate Life Insurance Company's Current Report on Form 8-K filed September 16, 2008.

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- 10.47 Reinsurance Agreement effective October 1, 2008 between American Heritage Life Insurance Company and Allstate Life Insurance Company. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed October 28, 2008.
- 10.48 Surplus Note between Allstate Life Insurance Company and Allstate Insurance Company dated November 17, 2008. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed November 18, 2008.
- 10.49 Investment Management Agreement between Allstate Investments, LLC and ALIC Reinsurance Company effective as of March 31, 2008. Incorporated herein by reference to Exhibit 10.1 to Allstate Life Insurance Company's Current Report on Form 8-K filed December 23, 2008.
- 23 Consent of Independent Registered Public Accounting Firm
- 31.1 Rule 13a-14(a) Certification of Principal Executive Officer
- 31.2 Rule 13a-14(a) Certification of Principal Financial Officer
- 32 Section 1350 Certifications
- 99 The Allstate Corporation Policy Regarding Pre-Approval of Independent Registered Public Accountant's Services effective February 23, 2009.

ITEM 15. (b)

The exhibits are listed in Item 15. (a)(3) above.

ITEM 15. (c)

The financial statement schedules are listed in Item 15. (a)(2) above.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

ALLSTATE LIFE INSURANCE COMPANY
(Registrant)

March 18, 2009

/s/ SAMUEL H. PILCH

By: Samuel H. Pilch
(Controller)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacity and on the dates indicated.

SIGNATURE

TITLE DATE

/s/ GEORGE
E.
RUEBENSON
President,
Chief
Executive
Officer
March 18,
2009 - ---

and a
Director
(Principal
Executive
Officer)
George E.
Ruebenson
/s/ JOHN
C.
PINTOZZI
Senior
Vice
President,
Chief
Financial
March 18,
2009 - ---

Officer
and a
Director
(Principal
Financial
Officer)
John C.
Pintozzi
Chairman
of the
Board and
a Director
March 18,
2009 - ---

Thomas J.
Wilson /s/
FREDERICK
F. CRIPE
Executive
Vice
President
and a
Director
March 18,
2009 - ---

Frederick
F. Cripe
/s/ DAVID
A. BIRD
Director
March 18,
2009 - ---

David A.
Bird /s/
MICHAEL B.
BOYLE
Director

March 18,
2009 - ---

Michael B.
Boyle /s/
DON CIVGIN
Director
March 18,
2009 - ---

Don Civgin
/s/ JUDITH
P. GREFFIN
Director
March 18,
2009 - ---

Judith P.
Greffin
/s/ SUSAN
L. LEES
Director
March 18,
2009 - ---

Susan L.
Lees /s/
JOHN C.
LOUNDS
Director
March 18,
2009 - ---

John C.
Lounds /s/
KEVIN R.
SLAWIN
Director
March 18,
2009 - ---

Kevin R.
Slawin /s/
DOUGLAS B.
WELCH
Director
March 18,
2009 - ---

Douglas B.
Welch

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
SCHEDULE I--SUMMARY OF INVESTMENTS
OTHER THAN INVESTMENTS IN RELATED PARTIES
DECEMBER 31, 2008

AMOUNT AT WHICH
COST/ SHOWN IN
THE AMORTIZED
BALANCE (\$ IN
MILLIONS) COST
FAIR VALUE

----- TYPE

OF INVESTMENT

Fixed

Maturities:

Bonds: United

States

government,

government

agencies and

authorities \$

2,792 \$ 3,687 \$

3,687 States,

municipalities

and political

subdivisions

3,976 3,308

3,308 Foreign

governments

1,652 2,100

2,100 Public

utilities 5,070

4,784 4,784

Convertibles

and bonds with

warrants

attached 957

973 973 All

other corporate

bonds 21,390

18,513 18,513

Asset-backed

securities

4,649 2,623

2,623 Mortgage-

backed

securities

2,923 2,719

2,719

Commercial

mortgage-backed

securities

5,712 3,730

3,730

Redeemable

preferred

stocks 15 9 9 -

Total fixed

maturities

49,136 \$ 42,446

42,446 -----

=====

Equity

Securities:

Common Stocks:

Public

utilities 1 \$ 1

1 Banks, trusts

and insurance

companies 36 19

19 Industrial,

miscellaneous

and all other

24 22 22 Non-

redeemable

preferred

stocks 45 40 40

-- Total equity

securities 106

\$ 82 82 -----

```

=====
-----
Mortgage loans
on real estate
10,012 $ 8,700
 10,012
=====
Policy loans
 813 813
Derivative
instruments 134
 $ 138 138
=====
Limited
partnership
interests 1,187
 1,187 Short-
term
investments
 3,855 $ 3,858
 3,858
=====
Other long-term
investments
 1,236 1,236 ---
-----
-----
Total
investments $
66,479 $ 59,772
=====
=====

```

S-1

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
SCHEDULE IV--REINSURANCE

```

PERCENTAGE
CEDED
ASSUMED OF
AMOUNT
GROSS TO
OTHER FROM
OTHER NET
ASSUMED ($
IN
MILLIONS)
AMOUNT
COMPANIES
(1)
COMPANIES
AMOUNT TO
NET -----
-----
-----
--- YEAR
ENDED
DECEMBER
31, 2008
Life
insurance
in force $
505,372 $
249,644 $
22,853 $
278,581
8.2%
Premiums
and
contract
charges:
Life and
annuities
$ 2,096 $
733 $ 48 $
1,411 3.4%

```


Accident
and health
179 141 47
85 55.3% -

Total
premiums
and
contract
charges \$
2,275 \$
874 \$ 95 \$
1,496 6.4%
=====

YEAR ENDED
DECEMBER
31, 2007

Life
insurance
in force \$
490,484 \$
244,827 \$
11,490 \$
257,147
4.5%

Premiums
and
contract
charges:
Life and
annuities
\$ 2,168 \$
804 \$ 42 \$
1,406 3.0%

Accident
and health
174 136 --
38 --% ---

--- Total
premiums
and
contract
charges \$
2,342 \$
940 \$ 42 \$
1,444 2.9%
=====

YEAR ENDED
DECEMBER
31, 2006

Life
insurance
in force \$
465,634 \$
236,278 \$
11,942 \$
241,298
5.0%

Premiums
and
contract
charges:
Life and
annuities
\$ 2,138 \$
639 \$ 45 \$
1,544 2.9%

Accident
 and health
 188 148 1
 41 2.4% --

 Total
 premiums
 and
 contract
 charges \$
 2,326 \$
 787 \$ 46 \$
 1,585 2.9%
 =====
 =====
 =====
 =====

(1) No reinsurance or coinsurance income was netted against premium ceded in 2008, 2007 or 2006.

S-2

ALLSTATE LIFE INSURANCE COMPANY AND SUBSIDIARIES
 SCHEDULE V--VALUATION ALLOWANCES AND QUALIFYING ACCOUNTS

ADDITIONS

 BALANCE AT
 CHARGED TO
 BALANCE AT
 BEGINNING
 COSTS AND
 OTHER END
 OF (\$ IN
 MILLIONS)
 OF PERIOD
 EXPENSES
 ADDITIONS
 DEDUCTIONS
 PERIOD ---

 --- YEAR
 ENDED
 DECEMBER
 31, 2008
 Allowance
 for
 deferred
 tax assets
 \$-- \$-- \$
 9 \$-- \$ 9
 Allowance
 for
 estimated
 losses on
 mortgage
 loans -- 3
 -- -- 3
 YEAR ENDED
 DECEMBER
 31, 2007
 Allowance
 for
 deferred
 tax assets
 \$-- \$-- \$--
 - \$-- \$--
 Allowance
 for

estimated
losses on
mortgage
loans -- -
- - - - -
YEAR ENDED
DECEMBER
31, 2006
Allowance
for
deferred
tax assets
\$-- \$-- \$--
- \$-- \$--
Allowance
for
estimated
losses on
mortgage
loans -- -
- - - - -

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the following registration statements of our report dated March 17, 2009, relating to the financial statements and financial statement schedules of Allstate Life Insurance Company (which report expresses an unqualified opinion and includes an explanatory paragraph relating to a change in method of accounting for uncertainty in income taxes and accounting for deferred acquisition costs associated with internal replacements in 2007), appearing in this Annual Report on Form 10-K of Allstate Life Insurance Company for the year ended December 31, 2008.

FORM S-3
REGISTRATION
STATEMENT
NOS. FORM
N-4

REGISTRATION
STATEMENT
NOS. -----

- 333-

- 100068 333-
- 102934 333-
- 112249 333-
- 114560 333-
- 119706 333-
- 114561 333-
- 121739 333-
- 114562 333-
- 121742 333-
- 121687 333-
- 121745 333-
- 121691 333-
- 121812 333-
- 121692 333-
- 125937 333-
- 121693 333-
- 129157 333-
- 121695 333-
- 143541 333-
- 121697 333-
- 150286 333-
- 150577 333-
- 150583 333-
- 156064 333-
- 157311 333-
- 157314 333-
- 157318 333-
- 157319 333-
- 157320 333-
- 157331 333-
- 157333 333-
- 157334

/s/ Deloitte & Touche LLP

Chicago, Illinois
March 17, 2009

I, George E. Ruebenson, certify that:

1. I have reviewed this report on Form 10-K of Allstate Life Insurance Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15(d)-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

March 18, 2009

/s/ GEORGE E. RUEBENSON

George E. Ruebenson
President and Chief Executive Officer

I, John C. Pintozzi, certify that:

1. I have reviewed this report on Form 10-K of Allstate Life Insurance Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15(d)-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

March 18, 2009

/s/ JOHN C. PINTOZZI

John C. Pintozzi
Senior Vice President and
Chief Financial Officer

SECTION 1350 CERTIFICATIONS

Each of the undersigned hereby certifies that to his knowledge the report on Form 10-K for the fiscal year ended December 31, 2008 of Allstate Life Insurance Company filed with the Securities and Exchange Commission fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that the information contained in such report fairly presents, in all material respects, the financial condition and result of operations of Allstate Life Insurance Company.

March 18, 2009

/s/ GEORGE E. RUEBENSON

George E. Ruebenson
President and Chief Executive Officer

/s/ JOHN C. PINTOZZI

John C. Pintozzi
Senior Vice President and Chief Financial
Officer

THE ALLSTATE CORPORATION

POLICY REGARDING PRE-APPROVAL OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANT'S SERVICES

PURPOSE AND APPLICABILITY

The Audit Committee recognizes the importance of maintaining the independent and objective stance of our Independent Registered Public Accountant. We believe that maintaining independence, both in fact and in appearance, is a shared responsibility involving management, the Audit Committee, and the Independent Registered Public Accountant.

The Committee recognizes that the Independent Registered Public Accountant possess a unique knowledge of the Corporation and its subsidiaries and can provide necessary and valuable services to the Corporation in addition to the annual audit. The provision of these services is subject to three basic principles of auditor independence: (i) auditors cannot function in the role of management, (ii) auditors cannot audit their own work; and (iii) auditors cannot serve in an advocacy role for their client. Consequently, this policy sets forth guidelines and procedures to be followed by this Committee when approving services to be provided by the Independent Registered Public Accountant.

POLICY STATEMENT

Audit Services, Audit-Related Services, Tax Services, Other Services, and Prohibited Services are described in the attached appendix. All services to be provided by the Independent Registered Public Accountant must be approved by the Audit Committee or the Chair of the Audit Committee. Neither the Audit Committee nor the Chair will approve the provision of any Prohibited Services by the Independent Registered Public Accountant.

PROCEDURES

In connection with the approval by the Audit Committee of the engagement of the Independent Registered Public Accountant to provide Audit Services for the upcoming fiscal year, the Independent Registered Public Accountant will submit to the Committee for approval schedules detailing all of the specific proposed Audit, Audit-Related, Tax, and Other Services, together with estimated fees for such services that are known as of that date. Subsequent to the Audit Committee's approval of audit engagement, Corporation management may submit to the Committee or the Chair for approval schedules of additional specific proposed Audit, Audit-Related, Tax, and Other Services that management recommends be provided by the Independent Registered Public Accountant during the audit and professional engagement period. Regardless of when proposed to the Committee or the Chair, each specific service will require approval by the Committee or the Chair before commencement of the specified service. The Independent Registered Public Accountant will confirm to the Committee or the Chair that each specific proposed service is permissible under applicable regulatory requirements.

Prior to approval of any specific Tax Service, the Independent Registered Public Accountant shall also provide to the Committee or the Chair a written description of (i) the scope of the service and the related fee structure, (ii) any side letter or other agreement between the Independent Registered Public Accountant and the Corporation or any subsidiary regarding the service, and (iii) any compensation arrangement or other agreement between the Independent Accountant and any person with respect to promoting, marketing, or recommending a transaction covered by the service.

As amended, effective February 23, 2009

THE ALLSTATE CORPORATION

POLICY REGARDING PRE-APPROVAL OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANT'S SERVICES

DELEGATION TO CHAIR

In addition to the Audit Committee, the Chair of the Audit Committee has the authority to grant approvals of services to be provided by the Independent Registered Public Accountant. The decisions of the Chair to approve services shall be reported to the Audit Committee at each of its regularly scheduled meetings.

REVIEW OF SERVICES

At each regularly scheduled Audit Committee meeting, the Audit Committee shall review a report containing (i) a summary of any services approved by the Chair since the Committee's last regularly scheduled meeting and (ii) an updated projection for the current fiscal year, presented in a manner consistent with the proxy disclosure requirements, of the estimated annual fees to be paid to the Independent Registered Public Accountant.

As amended, effective February 23, 2009

THE ALLSTATE CORPORATION

POLICY REGARDING PRE-APPROVAL OF INDEPENDENT REGISTERED PUBLIC ACCOUNTANT'S SERVICES

APPENDIX

AUDIT SERVICES

1. Annual financial statement audit
2. Review of quarterly financial statements
3. Statutory audits
4. Attestation report on management's assessment of internal controls over financial reporting
5. Consents, comfort letters, and reviews of documents filed with the Securities and Exchange Commission

AUDIT-RELATED SERVICES

1. Accounting consultations relating to accounting standards, financial reporting, and disclosure issues
2. Due diligence assistance pertaining to potential acquisitions, dispositions, mergers, and securities offerings
3. Financial statement audits and attest services for non-consolidated entities including employees benefit and compensation plans

TAX SERVICES

1. Domestic and international tax compliance, planning, and advice
2. Expatriate tax assistance and compliance

OTHER SERVICES

Any service that is not a Prohibited Service, Audit Service, Audit-Related Service, or Tax Service

PROHIBITED SERVICES

The following services, as more fully described in Regulation S-X, Rule 2-01, of the Securities and Exchange Commission, are Prohibited Services; provided however, that the services described in items 1 through 5 are not Prohibited Services if it is reasonable to conclude that the results of such services will not be subject to audit procedures during an audit of the Corporation's financial statements:

1. Bookkeeping or other services related to the accounting records or financial statements
2. Financial information systems design and implementation
3. Appraisal or valuation services, fairness opinions, or contribution-in-kind reports
4. Actuarial services
5. Internal audit outsourcing services
6. Management functions or human resources
7. Broker or dealer, investment adviser, or investment banking services
8. Legal services and expert services unrelated to the audit
9. Any other services that the PCAOB determines, by regulation, to impair independence

As amended, effective February 23, 2009